WORKPLACE PENSIONS REPORT 2014

LIFE FEELS BETTER WHEN YOU HAVE A PLAN

SCOTTISH WIDOWS

WORKPLACE PENSIONS ARE HAVING A POSITIVE IMPACT ON PENSION SAVINGS IN THE UK

FOR A LONG TIME, BRITONS HAVE FACED WARNINGS THAT THEY'RE NOT SAVING ENOUGH FOR RETIREMENT. OUR RESEARCH SHOWS THAT THIS PICTURE IS IMPROVING AND THE IMPROVEMENT IS DUE TO WORKPLACE PENSION SCHEMES, PARTICULARLY THE LAUNCH OF AUTOMATIC ENROLMENT IN OCTOBER 2012.

FOREWORD NEIL CARBERRY

CBI DIRECTOR, EMPLOYMENT AND SKILLS

LESS THAN 2% OF BUSINESSES HAVE GONE THROUGH THE STAGING PROCESS.

The beginning of this report says it all: pension provision is heading in the right direction. Businesses are at the helm, and though the journey has not been plain sailing, we are making good progress. But we've still got a long way to go, and to get there government and industry need to help smaller businesses navigate automatic enrolment.

It is good to see that the positive picture on automatic enrolment not only continues but is improving. This timely report from Scottish Widows shows that more people are aware of the new regime, more people are thinking about it positively and more are adjusting their saving plans accordingly.

This is an opportune moment for everyone involved in pensions to reflect on what business, government and savers are all looking to achieve: a long-term, sustainable pensions system. The changes to pensions announced at the Budget 2014 have reinforced the importance of getting automatic enrolment right and have given the industry new tools to ensure people can make the most of their retirement savings. But the report also highlights that there is still some way to go, in particular on guidance, advice and support for both businesses and their employees.

As this report concludes, the first priority must be to meet the demands of automatic enrolment. Less than 2% of businesses have gone through the staging process, and many of them have years of experience of handling pensions. A lack of knowledge of pensions – with all its idiosyncrasies and complexity – risks holding back SMEs unless they're well supported through the automatic enrolment process. Government, TPR, business organisations, and the pensions industry all have a major role to play in guiding them towards a result where millions of people are saving in good quality pension schemes. We must not lose sight of this in our ever changing pensions world.

A key piece of the automatic enrolment puzzle is communication and, at the moment, it doesn't quite fit. The findings in this report confirm what we have suspected for some time: that most people will want to know what they are getting at retirement and a good proportion of employees will look to their employer first for information about pensions. For businesses, pensions are increasingly important strategically both as a recruitment and retention tool and in long-term workforce planning.

There are clear opportunities here and at the heart of them is innovation. Scottish Widows' recommendations show that we all have a part to play. There are already good examples among businesses and the pensions industry, particularly around guidance and support for employees, but we need to get to a place where more of these practices are the norm rather than the exception.

Contents

WORKPLACE PENSIONS LANDSCAPE

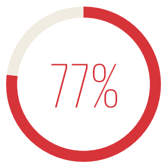
The Scottish Widows Workplace Pensions Report is based on an online survey of over 5,000 UK adults conducted by independent research agency, YouGov, in March 2014.

10 YEARS OF UK RETIREMENT FINDINGS

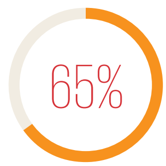
PEOPLE ARE ENGAGED WITH PENSION PLANNING

53%

Are saving adequately for retirement.



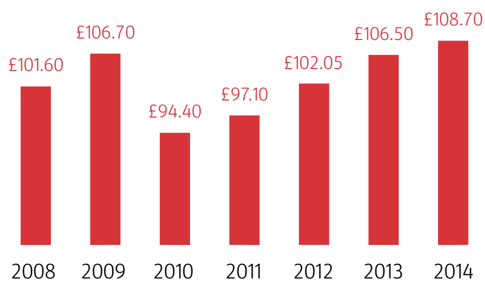
Number of people aware of automatic enrolment.



Number of people positive about automatic enrolment.

30%

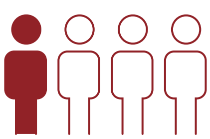
Employees say their pension is a major incentive to stay in their current job.



How much extra can you realistically afford to put aside each month for long-term saving?

Monthly savings figures are higher than they were pre-recession

EMPLOYERS, THE PENSION INDUSTRY AND THE GOVERNMENT NEED TO IMPROVE THEIR COMMUNICATIONS AND OFFER MORE ADVICE, GUIDANCE AND SUPPORT



1 in 4
Unaware of how much they contribute.

38%

Discussed pensions with their own adviser.

30%

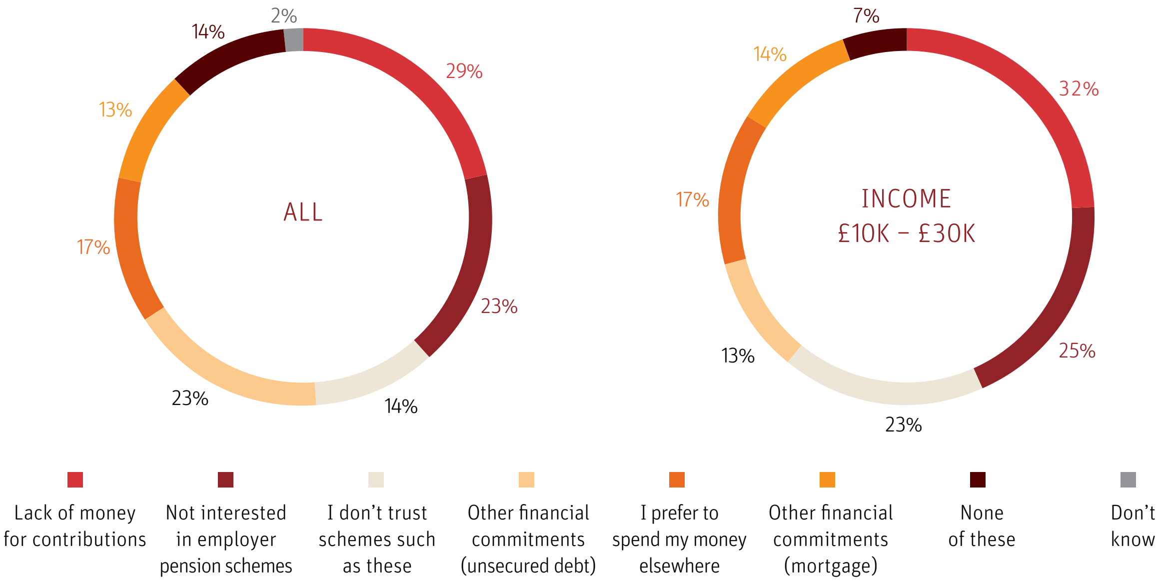
Willing to pay for pension advice.

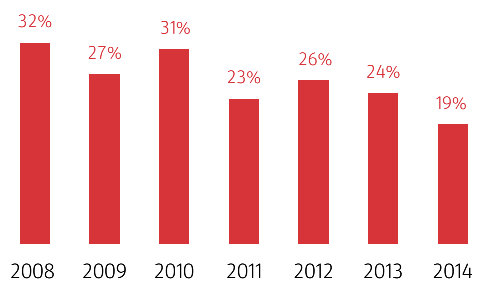
17%

Would turn to their employer first for information about pensions.

STRIKING A BALANCE BETWEEN LONG-TERM AND SHORT-TERM FINANCIAL COMMITMENTS REMAINS AN ISSUE FOR MANY

WHICH OF THE FOLLOWING, IF ANY, ARE THE REASON(S) WHY YOU'VE OPTED OUT OF AUTOMATIC ENROLMENT?





Are you likely to save more for the long term in the next 12 months?

For a long time, Britons have faced warnings that they're not saving enough for retirement. Our research shows that this picture is improving and the improvement is due to workplace pension schemes, particularly the launch of automatic enrolment in October 2012. Under automatic enrolment, over a six-year period, every employer in the country will be required to enrol their eligible employees into an occupational pension scheme and contribute towards it.

This type of intervention is having a positive impact on pension savings in the UK, and we hope this will continue following the more recently announced series of budget changes, which will see employees given much more freedom with how they take their pension benefits.

With more employers providing workplace pensions, and the improving economic outlook in the UK, people are already saving more for retirement. Our research shows that in 2014, 53% of people are saving adequately for retirement, a marked increase on last year, when the figure was only 45%, and the highest figure since 2009.

53%

Are saving adequately for retirement.

THE SCOTTISH WIDOWS PENSION INDEX SAVERS CATEGORIES

Non-savers

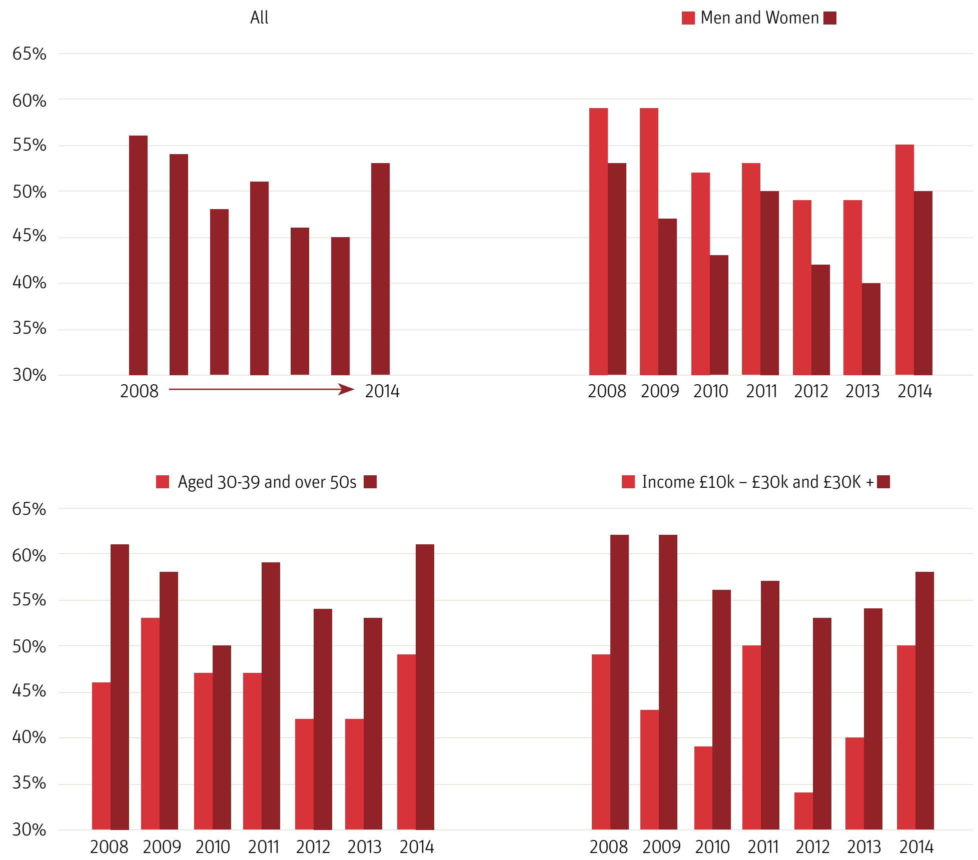
Serious under savers
putting away less than 6% of their income.

Somewhat under savers
setting aside between 6% and 12% of their income.

Adequate savers
saving 12% or more of their income.

See the Appendix on page 27 for an explanation of the Scottish Widows Pension Index.

THE NUMBER OF PEOPLE SAVING ADEQUATELY



Even stripping out those people who are fortunate enough to be members of a defined benefit pension scheme, preparedness for retirement is rising. 33% of people without defined benefit pensions are now saving adequately, up from 24% last year.

Some groups are doing much better than others. A typical adequate saver in 2014 is male, in his sixties, and working full-time. The typical inadequate saver is female, aged 30-39, with a lower household income and does not work. Almost a fifth of adults in the UK (19%), are still not saving at all, while a further 28% are saving less than they should. In other words, there are still many people in the UK, who remain vulnerable to a lack of retirement planning.

Nevertheless, pension provision is heading in the right direction. And if all pension stakeholders work together, targeting their focus where it is most needed, the more supportive economic backdrop now offers an opportunity to dramatically accelerate this positive trend.

01

AUTOMATIC ENROLMENT CLAIMS EARLY SUCCESSES

AWARENESS OF AUTOMATIC ENROLMENT IS 77%, UP 11% FROM LAST YEAR.

Two years after the Government revolutionised workplace pension provision in the UK, the architects of automatic enrolment are entitled to claim some major successes. A reform aimed at increasing the number of people making provision for retirement is achieving that objective: awareness of automatic enrolment is increasing, most people view the initiative very positively and opt-out rates are significantly lower than many predicted.

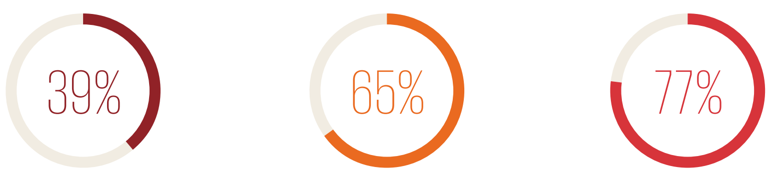
These findings are encouraging, for automatic enrolment has now entered a significantly more testing phase, with large numbers of small and medium-sized enterprises now reaching their staging dates (the date by which they must comply with legislation). This may explain the greater use of the National Employment Savings Trust (NEST) recorded in this year's survey – 11% of this year's sample has been enrolled in NEST, up from 7% in 2013, while the proportion enrolled through their employer's existing scheme has fallen from 71% to 59%.

As the reach of automatic enrolment extends, more people are becoming aware of it. More than three-quarters of people (77%) now say they are aware of automatic enrolment, up from 65% in 2013 and only 39% in 2012.

RESPONDENTS' AWARENESS OF AUTOMATIC ENROLMENT AND POSITIVITY

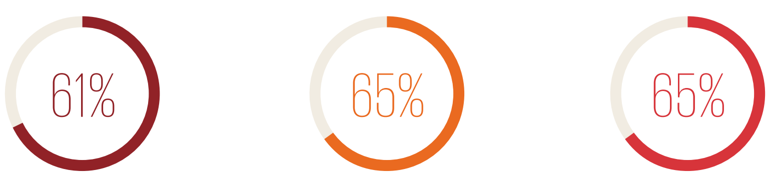
Number of people aware of automatic enrolment.

2012 2013 2014



Number of people positive about automatic enrolment.

2012 2013 2014



OPT – OUTS

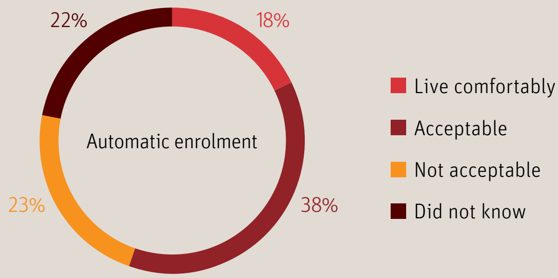
We asked people why they opted out of their employer's scheme after automatic enrolment. The top two reasons were lack of money (29%) and other financial commitments, such as credit cards and unsecured loans (23%). This shows that striking a balance between long-term and short-term financial commitments remains an issue for many.

On the other hand, among those people who do intend to stay in their employer's scheme, the amount they're prepared to contribute each month is rising. Some 30% expect to pay in between £25 and £50 each month, up from 15% in 2013, while 6% expect to pay in more than £200 each month, double last year's figure.

30%

Of people expect to pay in between £25 and £50 each month – double last year's figure.

IS AUTOMATIC ENROLMENT MAKING A DIFFERENCE?



Expected standard of living based on minimum contribution of 8%.

For those who weren't previously making pension provision, or didn't have access to a workplace pension scheme, automatic enrolment is making a positive difference.

We asked people how comfortable they would feel in retirement if they made only the minimum contribution of 8%. 18% felt they would be able to live comfortably, 38% felt they'd have a basic but acceptable standard of living, while 23% felt there would still be a gap they'd need to cover to get an acceptable standard of living – 22% didn't know.

For some, predominantly those on lower incomes, the automatic enrolment minimum of 8% may well be enough in retirement when combined with state benefits. While 8% savings is preferable to the previous situation where people were making no savings, we would maintain that saving 12% of income is needed to provide an adequate income in retirement.

Encouragingly, we found that 42% with a personal pension prior to automatic enrolment have continued to contribute to it and that looks set to be maintained. Amongst those waiting to be automatically enrolled who have personal pensions, 41% intend to continue making payments into them.
For many people, automatic enrolment represents only part of their savings for retirement, which is to be welcomed.

02

AUTOMATIC ENROLMENT THE TARGET MARKET

Automatic enrolment was designed with low and medium earners in mind – particularly the 70% of workers who, prior to the reforms, did not have access to a workplace pension scheme with employer contributions. By requiring all employers to provide a pension scheme for staff, and to make contributions on behalf of those who remain opted in, automatic enrolment has the potential to dramatically improve the retirement finances of many more people.

The good news is that the reforms are already having a notable impact on this target market. The number of younger people now seen as saving adequately has risen sharply – for those aged 30 to 49, the figure is now 49%, up 7% from 2013. Even better, the number of people on lower incomes – between £10,000 and £30,000 – now saving adequately has risen from 34% in 2012 to 50% this year. The number of women saving adequately now stands at 50%, up from 40% in 2013 – an encouraging increase for an important part of the target market for automatic enrolment.

HOW THE TARGET MARKET HAS RESPONDED

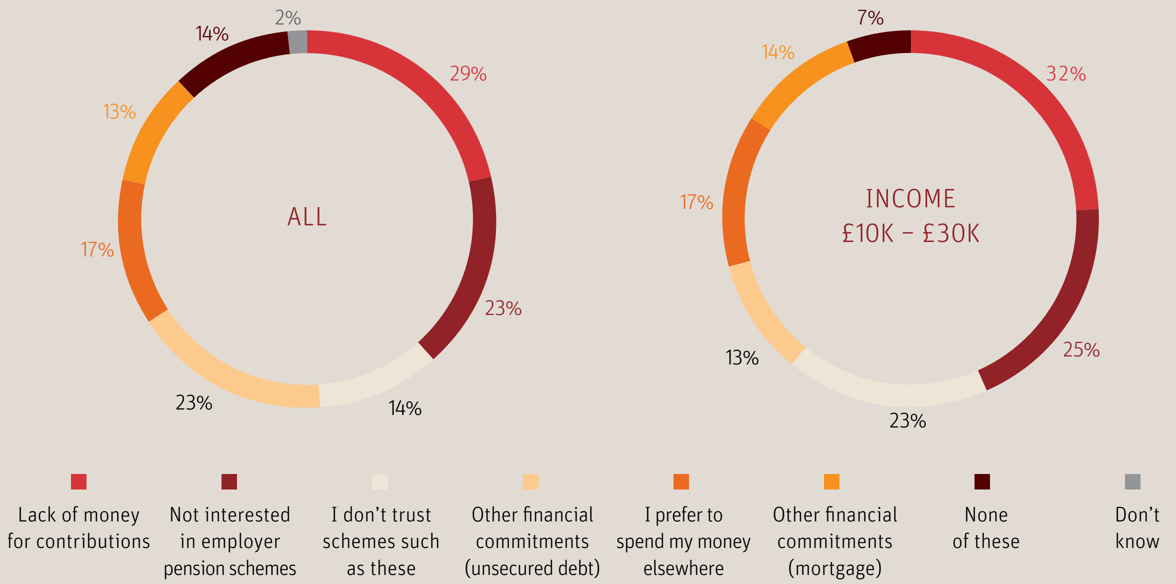
Those with lower earnings are more likely to think automatic-enrolment is a good idea: 70% of those with annual incomes between £10,000 and £20,000 are positive about the reform, rising to 79% for those with an income of between £20,000 and £30,000. This compares to 65% for all income earners.

50% OF WOMEN ARE NOW SAVING ADEQUATELY, UP 10% FROM LAST YEAR.

The story for younger workers is a little less positive, with 62% of 22-29 year-olds, rating the reform as a good idea. However, this is still a relatively encouraging figure given their likely prioritisation of commitments such as getting on the housing ladder or repaying debt.

Across the research, those who think automatic enrolment is a bad idea are most likely to justify this view on the grounds that people can't afford to contribute. This is also the most common explanation given by those who opt out. It appears that for many people in sectors where pay tends to be lower, automatic enrolment, even where it is seen as a positive initiative, may be considered unaffordable.

WHICH OF THE FOLLOWING, IF ANY, ARE THE REASON(S) WHY YOU'VE OPTED OUT OF AUTOMATIC ENROLMENT?



UNREALISTIC EXPECTATIONS?

Automatic enrolment is having a positive impact on many people in the target market, but it would be unfortunate if savers were given a false sense of security. When asked at what age people could start saving for retirement without jeopardising their standard of living in old age, a third (33%) said 25 or younger. But amongst younger people, only a fifth (21%) felt this was the cut-off point, suggesting they think they can wait until later to start saving.

It is also noteworthy that at a time when the state pension age is rising steadily, when asked at what age they would like to retire given their financial circumstances, younger people say around 62. People on lower incomes give broadly the same answer. In reality however, this might be an unrealistic expectation.

03

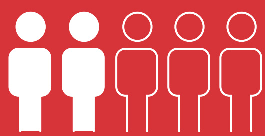
GET THE RETIREMENT INCOME YOU NEED

THE CHANCELLOR'S 2014 BUDGET ANNOUNCEMENTS ON PENSIONS TOOK PEOPLE BY SURPRISE, BUT HAVE THE POTENTIAL TO CHANGE THE RETIREMENT SAVINGS LANDSCAPE DRAMATICALLY.

From March 2015, no-one will be forced to buy an annuity; instead they will be free to continue investing their pension savings as they see fit and, subject to tax, to draw whatever income they want direct from their pension pots.

The freedom this will give pension savers has been broadly welcomed. But there are also fears that people will fall into the 'Lamborghini' trap; that they'll be tempted to withdraw all of their savings upfront and be left with no money for the rest of their retirement.

PEOPLE ARE PRUDENT



2 in 5 want a fixed annual income

1 in 2 would be comfortable managing their own pensions, investments and savings.

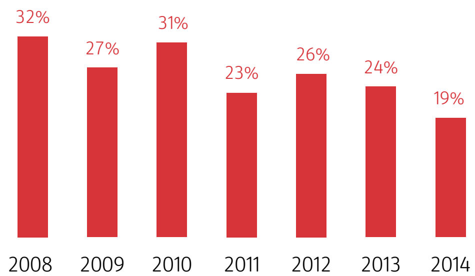
However, our research includes little evidence to suggest people will abuse the pension freedom they have been given.

Of those yet to retire, two in three (63%) say they want to know what their income will be in retirement, even if that means they end up getting slightly less. 41% of these people want a fixed annual income in retirement and a further 22% want an income in line with inflation. Only 6% would opt for a variable income.

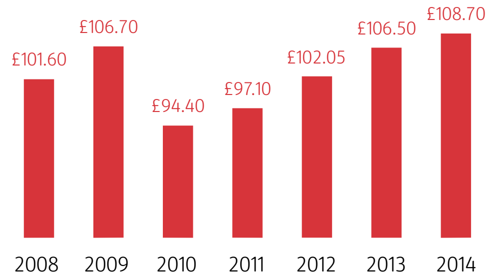
There will undoubtedly still be an appetite for avoiding annuity purchase. One in two adults (49%) say they would be comfortable managing the pensions, investments and savings they have accumulated for themselves. And those aged 55 or older are more likely than any other groups to feel this way. It is also the case that many people will not be wholly reliant on pensions in retirement: 20% intend to release cash from property in old age, while 38% have cash savings.

Nevertheless, when people were given a range of options for how they might cash in their pension savings, the most popular answer was the traditional route. More than a quarter of people (28%) would like to take some cash out of their savings to spend in the early years of retirement, with the rest of the money used to provide a guaranteed income for later years. It will be interesting to see whether this changes in years to come, as the 2014 Budget changes become a reality.

BUILDING AN ADEQUATE PENSION POT



Are you likely to save more for the long term in the next 12 months?



How much extra can you realistically afford to put aside each month for long-term saving?

In the years before savers reach retirement age and decide how to convert their pension pot into income, they must confront a more pressing issue: how to maximise the size of those savings. However, most people are struggling to increase their pension contributions. This year, just 19% said they were likely to start saving more for the long term at some point over the coming 12 months, down from 24% in 2013. Strikingly, those aged 40-59 are least likely to be able to save more.

Given the improving economic condition in the UK, we might have hoped to see a trend towards more people making higher contributions. But while the recession is over, incomes have yet to pick up steam, particularly taking into account the effect of inflation. And the squeezed middle remains much in evidence in pension savings.

More positively, amongst those who are intending to save more, the amount they intend to increase savings by is rising. Respondents were asked how much extra they could 'realistically afford to put aside each month for some kind of long-term savings'. The average amount is £108.70, a rise of just over £2 since last year.

The number of people able to save more may increase over the coming year, with incomes now finally beginning to pick up pace and inflation remaining low. This year, 35% of people expect to earn more, up from 31% in 2013. It's also encouraging to see that 11% claim to have a greater understanding of their financial needs in retirement and are saving more to support these.

04

PEOPLE NEED ACCESS TO INFORMATION, GUIDANCE AND ADVICE ON THEIR RETIREMENT SAVINGS PLANS.

ADVICE, GUIDANCE AND SUPPORT

The complexity of the pensions landscape, especially following the changes announced in this year's budget, makes it imperative that as many people as possible get access to information, guidance and advice on their retirement savings plans. Our research suggests that people are getting such support from a variety of sources – but also that they are reluctant to pay for financial advice.

Currently the Pensions Advisory Service (TPAS) is the most common source of information for people who want to find out more about pensions (27%), while another free service, the Money Advice Service, is also popular, with 21% stating this is their first choice. Friends and family are the preferred option for a further 21%, while 25% cite financial advisers.

The Retail Distribution Review (RDR) in 2013 promoted a shift towards fee-based financial advice and away from commission based charging. Our research showed that 30% of people would be willing to pay for pension advice. Of those who use financial advisers, 38% discussed pensions with their own adviser.

38%

Discussed pensions with their own adviser.

30%

Willing to pay for pension advice.

17%

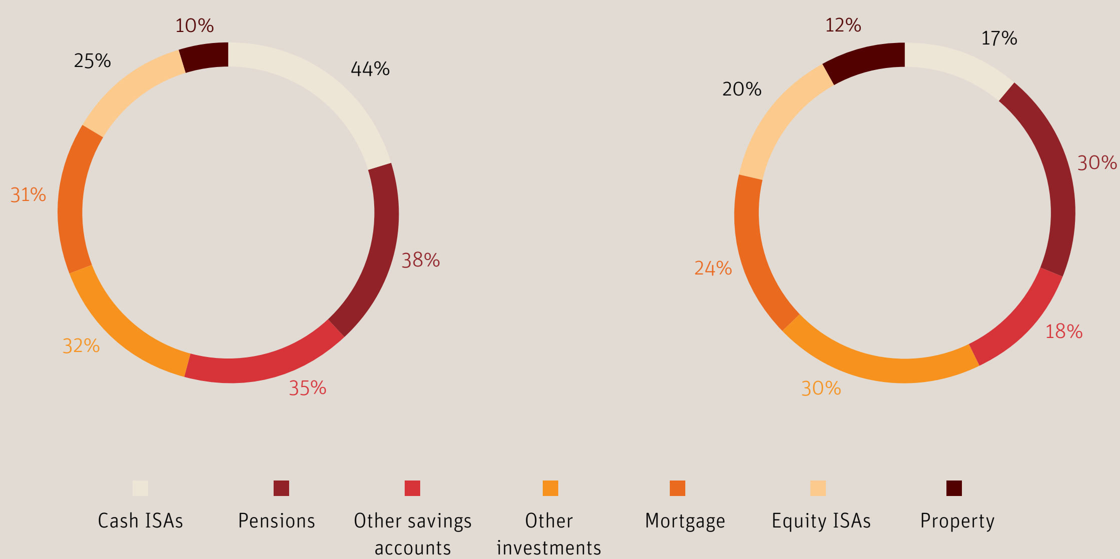
Would turn to their employer first for information about pensions.

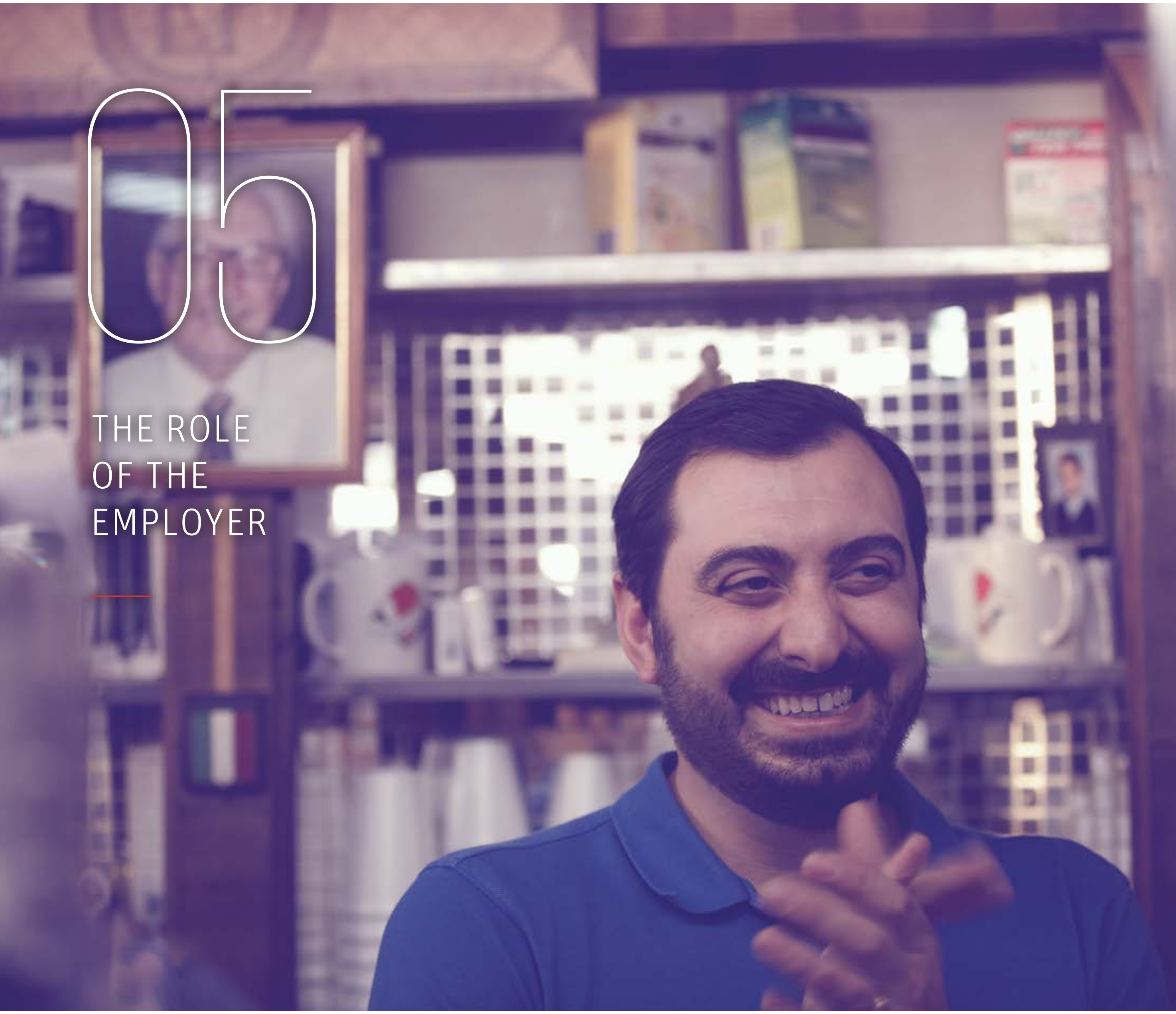
Demand for support in making workplace pension decisions is likely to increase, particularly as more people are automatically enrolled into workplace schemes. Already, 17% of people say their employer would be their first port of call if they were looking for information about pensions and we might expect that to increase as automatic enrolment progresses.

The 2014 Budget pledge to provide free and impartial guidance at the point of retirement will help, but planning for retirement is a 30-40 year journey, not a 45 minute conversation. Establishing a programme of information, guidance and advice throughout an individual's working life is key and will require government, pension providers, advisers and organisations such as The Pensions Advisory Service and Money Advice Service to work in partnership using multiple delivery channels. And, with the advice sector constricting in the wake of the RDR, the industry needs to look at introducing new types of lower cost and simplified advice for the mass market.

WHICH OF THESE PRODUCTS HAVE YOU DISCUSSED WITH YOUR FINANCIAL ADVISER?

WHICH OF THESE PRODUCTS WOULD YOU BE WILLING TO PAY FOR ADVICE ON?





05

THE ROLE OF THE EMPLOYER

EMPLOYERS ARE CRUCIAL STAKEHOLDERS IN THE DEBATE ABOUT HOW PEOPLE IN THE UK MAKE THE BEST POSSIBLE PLANS FOR RETIREMENT AND THE CHANGING PENSIONS LANDSCAPE HAS MANY FAR-REACHING IMPLICATIONS FOR THEM.

The first priority, particularly for employers that do not currently offer a workplace pension scheme, will need to be the immediate demands of automatic enrolment. Larger employers, which began reaching their staging dates in October 2012, have mostly coped well with automatic enrolment, but questions remain over the readiness of small and medium-sized employers, hundreds of thousands of which will come under the new system between now and 2018.

Several surveys of these employers have suggested that many are not leaving enough time to prepare for their staging dates – both in terms of selecting a pension provider in a competitive market, and in getting internal administrative and information technology systems and processes in place.

Help is available from professional advisers – though demand for their services is high – as well as from industry groups such as small business organisations. It will also be possible to learn from those employers that have already staged. However, only those employers that actively engage with automatic enrolment ahead of time can be confident of both complying with the requirements of the new system and offering a pension that employees value.

PENSIONS AS A RETENTION AND RECRUITMENT TOOL

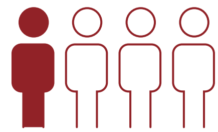
One question for employers to address is whether the quality of their pension schemes will be a more important factor in an era where people are increasingly concerned about how they will provide for old age. With all employers required to offer provision under automatic enrolment, will there be a move by employers to offer better pensions provision in order to attract and retain the best recruits?

30%

Of employees say their pension is a major incentive to stay in their current job.

When employees were asked whether their employer's pension scheme was a reason to remain in their current jobs, 30% said it was a major incentive. This is a rise of five percentage points from 2013 and may reflect the wider spread of automatic enrolment. Over time, this may feed through into the importance of pension scheme quality for new recruits.

It is important for employers to realise that the employer contribution offered is not the only factor in determining quality of the scheme. In particular, the standard of communication will be increasingly important as people seek more information and more support.



1 in 4
Unaware of how much they contribute

This should be a priority for improvement. Our research suggests many people currently have a poor understanding of their workplace pensions – for example, one in four (24%) do not know how much they are contributing to their pension scheme.

In practice, there are all sorts of ways to improve communication, even if employers stop short of offering access to full-scale financial advice, though some will want to offer links to professional firms. In some workplaces, individual and group meetings and printed material will be most appropriate. For others, digital channels such as email, the intranet and even social media can play a greater role. Online pensions education and information represents an important opportunity to add value to the employee offering.

THE CHANGING NATURE OF WORK

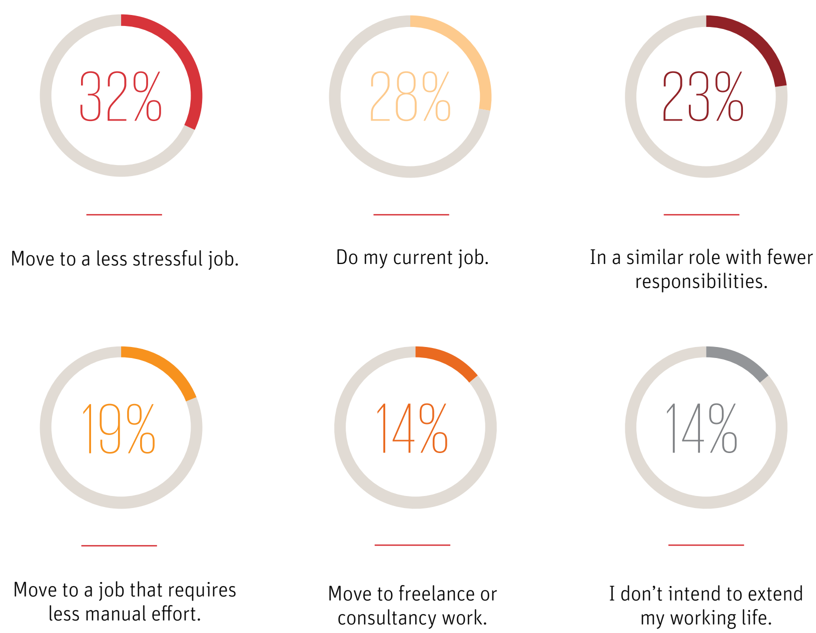
Employers will also need to consider the needs of older workers. As state pension age rises, and as people acknowledge that longer life expectancy demands greater financial provision, many will need or want to work longer.

Our research suggests people are already contemplating this possibility. Just 14% of people currently say they do not intend to extend their working lives. Of those that do intend to work longer, 53% say they will need to do so for financial reasons, but others say they will not feel ready for retirement (35%) or that they enjoy working and won't want to give it up (29%).

This is not to say, however, that people will want to carry on in the same jobs or continue working full-time. Many are contemplating a move into different types of work, while 67% look forward to reducing their hours or working more flexibly.

Employers will need to think carefully about how to accommodate people's wishes as they reach the age during which employees traditionally retire. Succession planning may also be an issue – will younger people get the career progression they desire if their older colleagues remain in work?

IN WHICH OF THE FOLLOWING WAYS WOULD YOU EXTEND YOUR WORKING LIFE?



06

RECOMMENDATIONS

Our research paints an encouraging picture of workplace pension provision in the UK today.

Individuals are engaged with pension planning, employers are coping well with automatic enrolment, the pensions industry is providing innovative new solutions and the Government recognises the need for supportive policy. The result is that the number of people now saving adequately for retirement is increasing.

Nevertheless, there is plenty of room for improvement – each of these key stakeholders needs to do more.

EMPLOYERS MUST...

1. Prepare for automatic enrolment if not there yet – for those employers yet to reach their staging dates, getting ready to stage, and shopping around to find the best possible pension scheme for their workforce should be the priority. This will mean putting compliant pension provision in place (including debating how generous to be) and ensuring they make the relevant changes to technology solutions and administration services. They should ensure that employees understand what is available in time to make an informed decision about contribution levels;

2. Consider their role in pension advice and support – employers will not generally be able to offer independent financial advice in the workplace, but with employees looking to them for help, the more information they can provide the better. Digital channels, such as education and guidance portals provide a valuable opportunity to do much more on this issue;

3. Focus on communications – too few employees currently understand what their workplace pension scheme offers. This undermines their ability to plan for retirement, but also means they may have little appreciation of a crucial part of their remuneration and rewards package.

INDIVIDUALS MUST...

1. Confront the need for pension planning - our research shows people want to retire at 62, but the state pension will not start until 65 or later over the coming years. Only private pensions can close this gap.

2. Establish their current level of pension provision – seeking out better information about what pension savings they currently have, and what these will be worth at retirement, is the best way for people to consider whether they are making adequate provision for old age;

3. Review the need to save more – the majority of people need to save more for retirement and many people say they have the ability to increase their contributions. They should consider doing so now, either through their workplace pension or some other type of pension provision.

THE PENSIONS INDUSTRY MUST...

1. Continue to offer innovation that supports employers – automatic enrolment is placing a strain on employers and the pensions industry is in a position to help. Imaginative, good quality product offerings that meet customers' needs, will enable many employers to do more than the minimum required by the new system;

2. Work with employers to plug the information and advice gap – there is a role for the pensions sector to provide more advice through independent professionals, but with many people likely to turn to employers for such support, the industry also needs to help workplace schemes meet this need. Digital channels will play an increasingly important role;

3. Improve the support it offers savers by responding to the 2014 Budget changes - delivering products and services that give customers greater flexibility to access their pension savings and support in making the right decisions.

GOVERNMENT MUST...

1. Make it easier for people to get the support they need to plan and prepare for retirement. This can be achieved by setting out clear parameters for each party involved - from employers to professional advice and guidance services as well as product providers;

2. Look at options for introducing new types of lower cost and simplified advice and guidance for the mass market. The Government's Freedom and Choice in Pensions proposal has removed the default retirement routes for many. As a result we expect to see an increase in the number of people requiring advice at retirement. We'd like to see the Government work with Guaranteed Guidance providers to develop a 'Retirement Passport' as an output. This should contain an agreed set of relevant retirement information – such as pension policy information, family circumstances, basic health information and retirement aspirations. This could speed up the guidance process and reduce the costs of the handover to regulated financial advice; or indeed be the entry point into a new lower cost focused or simplified advice route;

3. Recognise that providers, and the wider industry, need time to implement all the legislative changes currently in the pipeline and support them in developing innovative solutions to meet the needs of future retirees.

APPENDIX

THE PENSIONS INDEX AND THE AVERAGE SAVINGS RATIO

Calculation of the Pensions Index

The Scottish Widows Pensions Index is a snapshot of how well employed and self-employed people in the UK are currently preparing financially for retirement. It is based on those who are of an age – between 30 and 64 (men) / 59 (women) – and an income level – £10,000 or more a year – where they could reasonably be expected to be saving for their old age. The target retirement income is one that will leave most people feeling they are in an acceptable financial position, but which is likely to involve a sacrifice in living standard compared with when they were working. The level of retirement income which consumers are likely to feel is acceptable will depend largely on their income while working. However, the proportion required is likely to be higher for lower earners than for those who are relatively well-off, and that is reflected in our assumptions.

We have assumed that saving 12% of earnings from age 30 to age 64 will provide an adequate income when combined with state pensions. The 12% includes employer pension contributions, tax relief and any non-pension savings for retirement, and could produce a pension of around 17% of earnings at age 65, based on projections using the pensions calculator of the Money Advice Service. When added to a state pension of £7,500 a year (assuming at least 35 years of NI contributions or credits), those earning £10,000 a year and saving 12% a year may have an income replacement rate of around 92% in retirement, those earning £30,000 may have a replacement rate of around 42%, and those earning £50,000 may have a replacement rate of around 36%.

If individuals continue to work and contribute to pension until state pension ages when these increase above 65, these replacement rates will be increased significantly.

Those with defined-benefit pensions need to be considered separately, because there is no direct relationship between contribution levels for individuals and the pension provided. In calculating the Index we have assumed that all those who expect to receive most retirement income from a defined-benefit pension are adequately provided for. The Scottish Widows Pensions Index therefore tracks the percentage of those aged between 30 and 64 (30 and 59 for women) and earning £10,000 or more a year who are either relying mainly on a defined-benefit pension or saving at least 12% of earnings for their retirement (including any pension contribution by their employer). The Scottish Widows Average Savings Ratio is the average percentage of earnings being saved for retirement by those in the Index group, but excluding those relying mainly on a defined-benefit pension.

For the past two years we have calculated an alternative index which includes women aged 60 to 64. This extra group has not affected the outcome for either of our main measures, largely because relatively few women over age 60 were still earning.

Savings that are included

While pension arrangements remain the most common and most tax-efficient method of saving for retirement, many people use alternative savings vehicles such as ISAs, perhaps with a view towards moving funds into pension closer to retirement. In calculating the Pensions Index and the Average Savings Ratio, we have taken account of all savings specifically intended to contribute towards retirement income. These comprise company and employee contributions to employer-sponsored pensions, individual contributions to personal and stakeholder pensions and non-pension savings. We have not included non-financial assets such as residential property.

SCOTTISH WIDOWS

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