Why you shouldn't bet on a state pension

A growing population means you might have to wait longer to retire

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A review of state pension age is about to wrap up and many fear that they may have to work longer or face a less comfortable retirement. The state pension age is already due to rise from 66 to 67 by 2028 and to 68 by 2046, and any further changes could derail millions of retirement plans. Here's what you need to know.

Why is state pension age going up?

Because it is unaffordable for the government. State pension age was set at 65 in 1926 and lowered to 60 for women in 1940. A person born in the 1920s had a life expectancy of about 70. Today, people live over a decade longer on average and often spend more than 20 years in retirement. The state pension costs over £100 billion a year.

It is effectively a Ponzi scheme — it relies on having enough working-age people paying taxes to provide pension income for the older generation. In 1926, there were nine working-age people for every retired person in the UK. Today the ratio is more like three to one.

Increases in state pension age are linked to life expectancy. By 2028 a 67-year-old man reaching state pension age will be expected to live a further 18.7 years and a 67-year-old woman another 20.8 years.

Who will be affected?

If the state pension age goes up earlier, the people most likely to see their pension age change are those in their late forties to mid-fifties. Those in their mid-forties and below are already on track for a state pension age of 68 or older. Under present plans, anyone born on or before April 5, 1977 will have a state pension age of 67. Those born after April 6, 1978 will have a state pension age of 68. The state pension age for those born in between will be between 67 and 68.

If this is accelerated and the state pension age rises to 68 by 2039, as was called for in an official review in 2017, this will change. According to the wealth manager AJ Bell, anyone born on or before April 5, 1970 would get the state pension at 67. Those born after April 6, 1971 would get it at 68. State pension age would be staggered for those in between.

Nothing has yet been confirmed and the government has previously said it would give ten years' notice of any changes. It was widely criticised for not communicating the increase in women's state pension age to 66 effectively.

A review is carried out every five years and the latest one is being completed. Steve Webb, a partner at the consultancy LCP and a former pensions minister, said: "Life expectancy has not improved since the last review so in my view there is no case for a faster pace of increases."

Are there any benefits?

The main benefit is to the Treasury, which would save about £10 billion a year by raising state pension age sooner.

Adrian Lowery, from the wealth manager Evelyn Partners, said: "It is difficult to see the upsides for pensioners except that if it makes the guaranteed state pension more sustainable then that is obviously good for younger people."

What are the downsides?

The main downside is that you would lose out on a year of state pension income. From April, this would be worth £10,600. If the state pension increased 2.5 per cent a year then by 2046 it would be worth about £18,700 a year.

Another issue is planning. Many who want to stop work at a certain age may have to make their private pension stretch further. Others will have to work longer or put up with a less comfortable lifestyle in retirement.

According to Interactive Investor, an investment platform, someone retiring with a £100,000 pension pot could run out of savings at 79 rather than 81 if they needed to withdraw an extra £10,600 to cover a year's lost state pension income.

Life expectancy varies according to region, wealth and health conditions. Those with a lower life expectancy may feel short-changed because they will not receive the benefit for as long.

Will it affect how much I get?

It will not affect your annual income once you reach state pension age, but you would miss a year of income.

Lowery said: “However, you are still likely to be getting more years’ state pension income than someone who was born 20 or 30 years ago.”

Is there anything I can do?

Saving into a private or workplace pension scheme is vital. The earlier you start, the better.

Tom Selby, head of retirement policy at AJ Bell said: “It would not be surprising if those in their twenties and thirties today have to wait until their 70th birthday or beyond to get the state pension.”

According to Interactive Investor, saving £200 per month in your pension for 40 years could give you a retirement income of about £18,000 a year, assuming 5 per cent investment growth.

Those who are closer to retirement age could explore equity release to unlock wealth from their home.

Make sure that when you do reach state pension age, you are entitled to the full amount. Check your National Insurance record with HMRC. You need 35 years of contributions to qualify at present. This can be a particular problem for women who have taken career breaks to raise a family or care for relatives. Voluntary contributions can help you to boost your retirement income.

Is it happening elsewhere?

Not every country offers a state pension, but those that do are having the same dilemma. There has been uproar in France over plans to raise the state pension age from 62 to 64.

The set up varies between countries — the UK pays a flat rate of state pension but in Germany, for example, your state pension is set using a points system based on your earnings. The present state pension age is 65 and rising to 67. In the Netherlands there is a flat rate system, and the retirement age is 66 years and ten months, rising to 67 by 2025.