FINANCE UPDATES

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CAMPBELL & McCONNACHIE
chartered financial planners

CAN YOU AFFORD TO LIVE TO 100?

Increasing longevity equates to longer retirement.

Going back 30 or 40 years, retiring at the age of 65 and living off of your state pension for the rest of your life was doable.

Mind you, life expectancy was much lower in the 1980s. For example in 1988, the average male could expect to reach 72 while the typical female would make their 78th birthday.

Fast forward to 2018 and the Office for National Statistics (ONS) said the average male lived for seven years longer than in 1988 and the typical female was around for five more years.

It's clear to see that living off the state pension is extremely unlikely for most people in 2020 and traditional estimates of the ideal amount for a comfortable retirement are falling short.

While increasing longevity is a good thing, it also presents challenges. According to a report from the World Economic Forum, the UK's retirement savings gap stood at £8 trillion in 2015, and that chasm is expected to widen to £33tn by 2050.

People in the UK, the report claimed, should expect to live eight-and-a-half years longer than the pot of money they have saved for retirement, with the highest burden on women.

The odds of getting a 100th birthday card from a future King or Queen are 50/50 for a 20-year-old in the UK today.

By 2050, reaching this milestone will be far less rare, so what do you need to consider and which sources of retirement income will help you reach your century?

ARE THERE PENSION OR SAVINGS CAPS?

In 2019/20, you have an annual pension contributions allowance of £40,000 and a pension lifetime allowance of £1.055 million.

Indications are the first figure will remain in place from April, while the latter figure – subject to Government rounding – will rise to £1.075m for 2020/21 in line with last September's Consumer Prices Index rate of inflation.

It's important to note the differences between contributions and values with both of these limits. Contributions are what you can put into your pension each year, while the value of your pension can grow over time if it performs well.

You can bring forward any of your unused annual allowance as long as the amount you paid into your pension in one of the three previous years was less than £40,000.

Using your £20,000 annual ISA allowance is another tax-efficient way to build up savings for a long retirement as any growth and withdrawals will be tax-free, unlike withdrawals from your pension that are taxed at your marginal rate if it exceeds the personal allowance.

If you've fully used your annual ISA and Self-Invested Personal Pension allowances, you can still invest in funds and shares.

Any income or gains may be subject to income and capital gains tax, although you do have your annual personal allowance, dividend allowance and capital gains tax allowance to use first.

START SAVING YOUNG

The key to any long-term savings strategy is to start young. If you're over the age of 22 and earning more than £10,000 a year, you can get the ball rolling with a workplace pension.

This usually requires you putting at least 5% of your salary into a pension, while your employer is obliged by law to contribute a minimum of 3%. Both parties can put in more if they choose.

Based on current projections, those in their 20s right now are likely to retire sometime in their mid-2060s.

Estimates suggest placing around 13% of your pre-tax salary each year into a pension from the age of 25, although this percentage increases the longer you wait to start saving.

STATE PENSION

Then there's the new state pension. Currently, 35 full years of national insurance contributions (NICs) entitle you to £168.60 a week, or £8,767.20 a year, that goes towards your retirement.

There is an elephant in the room with NICs, though, as the UK's ageing population puts the National Insurance Fund under strain.

A report last year by the Government Actuary's Department predicted the fund would be empty by around 2032.

If someone was to retire today at 65 on April 2019's average annual salary of £30,000, and they receive a full (new) state pension of £8,767.20, they would need to generate around £21,000 a year from their private pension pot to maintain their quality of life before becoming a centenarian.

LIFETIME ANNUITIES

On top of drawing a full new state pension of £168.60 a week, you have a plethora of options when it comes to how you access your savings at retirement.

One option to consider if you think there's a chance of you reaching your century is a lifetime annuity, which may offer a guaranteed income for the rest of your life.

When you're nearing retirement and have a clear date in mind, you can purchase one of these products and get the income paid monthly, quarterly, biannually or annually, and receive it in advance or arrears.

However, these products also generally offer very poor value for money as the effective rate of return is low.

The income is also flat unless you build in an index factor, which will increase the income every year. But this costs a lot more and so your income will start from a lower level.

SHOULD YOU CONTINUE WORKING?

The UK's employment rate is currently at a record high of 76.3%, according to the most recent labour force figures from the ONS.

When you dig beneath the headline figure, it becomes clear the UK's booming employment rate is almost entirely driven by older workers. In particular, changes to the state pension age for women have resulted in fewer women retiring between the ages of 60 and 65.

Even though those working into their 60s will no longer be paying NICs that count towards state benefits, adopting a more phased approach to retirement can top up your pension pot when the time comes to access it.

As each generation lives for longer, it's inevitable they will need to work longer to fund their retirement. That's particularly true when you consider that the number of valuable final-salary pension schemes is dwindling and the defined contribution schemes are considerably less generous.

Research from Canada Life last year claimed more than 23 million savers are braced to work beyond the age of 65, with many admitting they need to continue to earn a wage due to insufficient pension savings.

Having established the need to generate around £21,000 a year from your private pension pot, £743,000 would be needed in 2019 just to fund a 65-year-old retiree until their 100th birthday.

That's before taking into account rising costs of living and the potential for prolonged spells of low interest rates.

Fortunately, you can avoid working past the age of 65 by seeking expert independent financial advice to come up with an efficient retirement plan to last if you're blessed with longevity.

We can help you form a retirement plan.