

Perceptions of income requirements in retirement

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Background and research objectives

The last ten years have seen a high level of public debate and policy development around the subject of pensions and the financial situation for people post-retirement. A recent report by the Pensions Policy Institute suggested that *'many people felt they would need to have a standard of living similar to working life, in order to be satisfied with their retirement income'*.¹ However, what was not known in any detail was how people determined what was an appropriate retirement income. To address this, a qualitative study was undertaken to explore:

- individuals' views about their current financial situation and standard of living in retirement and their feelings about their financial future;
- what factors influence individuals' views about their current financial situation, including their perception of appropriate retirement income and wealth;
- the influence of 'replacement rates' on individuals' feelings about their financial situation. The replacement rate is a calculation of the ratio between earned income before retirement, and income in retirement;
- the factors that may have created a disjunction between aspirations for retirement and actual income and wealth in retirement.

Research design

The study comprised 30 in-depth interviews with respondents drawn from the English Longitudinal Study of Ageing (ELSA). All respondents had been retired from their main job for at least two years, had been earning between £10,000 and £40,000 in their last main job and had some pension income over and above the State Pension. Respondents were purposively selected based on two key criteria: age (60-69 and 70-77) and replacement rate of income pre- and post-retirement.

The income replacement rates for eligible ELSA respondents were calculated in a similar way to those defined in the Pensions Commission report². This involved dividing an individual's gross retirement income (from pensions, benefits, savings and investments, etc.) by their gross earnings pre-retirement (i.e. their final salary before tax). However, this study used 'current' retirement income (i.e. at the point of the interview) whereas the retirement income definition used in the Pensions Commission report was income at the point of retirement. To get an individual retirement income for calculating the replacement rate, if relevant, a couple's joint retirement income was divided by two.

A quantitative analysis of the sub-sample of 613 eligible ELSA respondents from which the qualitative sample of 30 was drawn indicated that the median replacement rate was 54 per cent.

The research was carried out on behalf of the Department for Work and Pensions (DWP) by the National Centre for Social Research (NatCen).

¹ *Retirement income and assets: Do pensioners have sufficient income to meet their needs?* (2009).

² *Pensions: Challenges and Choices. The First Report of the Pensions Commission* (2004).

Definition of different lifestyles in retirement

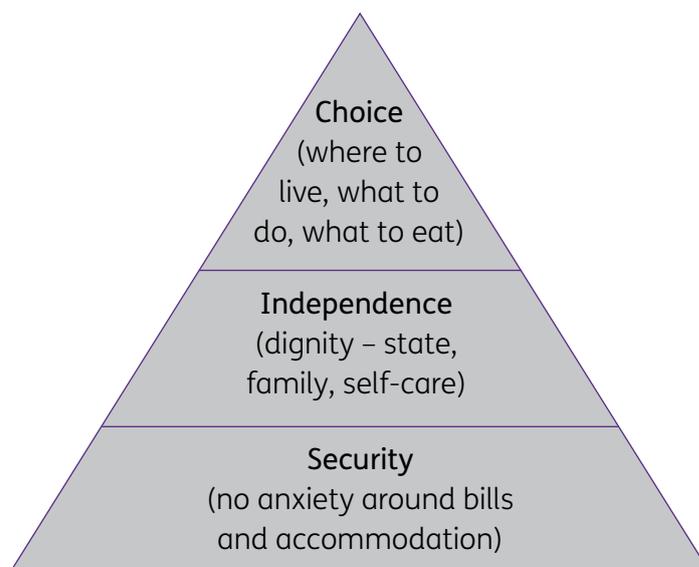
Respondents identified three categories of lifestyle in retirement: 'basic', 'comfortable' and 'wealthy'. There were three key components informing the definition of these various lifestyles: security, independence and choice, as illustrated in the diagram below.

Security was the most basic need expressed by respondents and related to the absence of anxieties around being able to afford to pay bills (e.g. heating bills), dealing with financial emergencies (e.g. if key white goods such as a refrigerator broke down) and having secure accommodation. The concept of independence was related to respondents being able to manage with the least financial and caring assistance from the state (in terms of benefits) and from family, and being generally able to manage their own self-care.

Whereas security and independence were linked to having the income to secure the basic prerequisites of lifestyle, choice related to respondents having the income to be able to **enhance** their quality of life. This included considerations around frequency of holidays and other leisure activities, quality of food and the type of accommodation someone could afford to live in.

A 'basic' lifestyle was seen to be one which lacked financial security and independence and was therefore seen to be characterised by anxieties around being able to afford to pay bills and replace household goods, as well as financial dependence on friends, family and state benefits.

In contrast, a 'comfortable' lifestyle was seen to begin at the point of financial security and independence. However, there was a great deal of variation within this lifestyle in terms of the level of choice respondents felt that they had to enhance their quality of life.



The difference between a 'wealthy' lifestyle and a 'comfortable' one rested on the ability of those in a 'wealthy' lifestyle to exercise choice on a grander scale (e.g. being able to afford to live in expensive properties).

Perceptions of own lifestyle

Respondents tended to distance themselves from both the 'basic' lifestyle, which was associated with media images of 'pensioner poverty', and a 'wealthy' lifestyle, which was associated with a 'frivolous' and 'extravagant' living.

Instead, respondents generally identified with a 'comfortable' lifestyle, which may, in part, be because the sample excluded those who were on pre-retirement incomes of less than £10,000 and above £40,000. This tendency to identify with a 'comfortable' lifestyle accounts for why there was a wide variation in how respondents defined this lifestyle. This variation can be made sense of by further segmenting this lifestyle into the categories of 'marginally comfortable', 'moderately comfortable' and 'very comfortable' based on how tightly respondents needed to budget in order to exercise lifestyle choices and whether they felt they needed additional income.

In defining their own lifestyle (as well as the lifestyle of others), respondents not only drew on media images (largely of 'pensioner poverty') and other people (including family, friends, neighbours and former work colleagues) but also their own experiences before retirement and their current attitudes towards spending and money management – which tended to frame the discussion of a 'comfortable' lifestyle around being careful with money and not being frivolous.

Respondents' feelings about their retirement income and their lifestyle were influenced by both financial and non-financial factors. Although it was not possible to identify in what way replacement rates specifically had an influence on feelings about retirement incomes, other financial factors did play a part in shaping these feelings. These included current household income, whether they owned their property and had paid off their mortgage and the level of savings and debt they had. In particular, the ownership of property and the absence of debt contributed to respondents feeling better off in retirement in comparison to their working lives, even though their income may now have been lower.

The following non-financial factors also contributed to feelings about lifestyle so that, as long as basic levels of security were met, respondents felt positive about their lifestyle regardless of their income:

- **Attitudes towards spending:** Respondents displayed the ability to tailor their expectations, expenditure and needs to match their income.
- **Aspirations in retirement:** Tailoring aspirations to age, with one view being that ill health and/or ambitions being fulfilled in working life meant that individuals needed less income in retirement.
- **Health and mobility:** Good health was seen to give individuals the capacity to enjoy their retirement and to limit costs associated with ill health (and hence, income needed).
- **Support networks:** A good support network of friends and family was seen to make life in retirement more comfortable because of the emotional and material support they offered.

Views about the future

The recurrent view among respondents was that their income and assets would not increase substantially in the future, over and above any minor adjustments made to their pensions and any changes in interest rates that could affect savings, bonds and other investments.

Respondents described a number of threats to their financial wellbeing both in terms of their level of income and assets and the changing nature of the demands placed on their income. Some of these threats related to their current situation, while others were seen to be potential threats in the future (e.g. the death of a spouse or government cuts in entitlements).

One such threat was the potential demands placed on respondents' finances as a result of a deterioration of their (or their partner's) health and mobility as they got older. These demands included the costs of care and other assistance that would be required.

Respondents were also concerned about the effect of inflation in eroding fixed pension income and assets, both now and in the future. As a way of meeting this threat, respondents felt that they would need to draw on savings, investments and/or reluctantly consider selling their property and downsizing.

Respondents tended not to have any concrete plans for the future, with the recurrent view being that they would keep drawing on their current income and asset streams without any further planning. Reluctance to think about future planning was based on perceived limitations that a fixed retirement income placed on financial planning, a reluctance to think about unpleasant issues that may require planning (especially the deterioration of health) and not seeing the point of planning given that respondents did not know how long they would live.

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The full report of these research findings is published by the Department for Work and Pensions (ISBN 978 1 908523 20 4. Research Report 773. September 2011).

You can download the full report free from: <http://research.dwp.gov.uk/asd/asd5/rrs-index.asp>

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