FINANCIAL TIMES

Can you afford to live to 100?

Financial innovation has not kept up with life expectancy. How will you fare?

JULY 27, 2017 by: Lindsay Cook

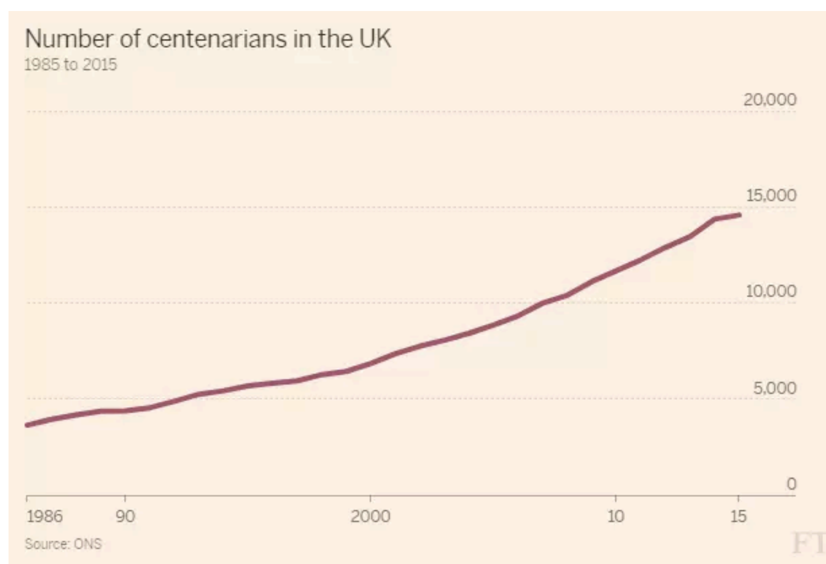
When Otto von Bismarck launched the first state pension in Europe in the 1880s, only 1 per cent of the German population lived to collect it. Qualification for payment was carefully set at 70; the founder of the world's pioneering welfare state had done his actuarial sums.

Today, many pensioners can expect to live for decades longer. The number of people reaching the age of 100 has quadrupled in the past 30 years and is likely to quadruple again by 2035. Increasing numbers of 100th birthday celebrations means the government has expanded the team sending telegrams from the Queen to seven employees.

It will be considerably harder to resolve the complex financial challenges that rising longevity presents. Only last week, the government announced it would accelerate the planned increase in the state pension age to 68 for millions of people born between 1970 and 1978 — a move projected to save £74bn. Its shrunken parliamentary majority can partly be blamed on the uproar over a "dementia tax" to fund the rising cost of social care. The policy has been dropped — but the problem has not gone away.

Unless radical changes are made, it is almost certain that most people will not be able to save enough to fund several decades of retirement as we know it. But the concept of retirement is changing fast and our long-term financial plans must adapt accordingly.

Working for longer can reduce the "longevity risk" of our pensions and investments. Younger workers should consider saving a higher proportion of their incomes. But good financial planning also involves flexibility. The risk of running out of money must be weighed against dying with too much and incurring large inheritance tax bills.



When it comes to selecting financial products that can help us achieve this balance, innovation has not kept pace with rising life expectancy. Rather than wait for what the finance industry, regulators and politicians come up with, here is our guide to assessing your finances in later life:

A child born in the developed world today has a more than 50 per cent chance of living to be over 105, say Andrew Scott and Lynda Gratton, professors at London Business School and authors of The 100 Year Life: Living and Working in an Age of Longevity.

Those aged 30 today have a 50 per cent chance of living to more than 100. At 50, you have even chances of reaching the age of 95. At 60, you have a 50 per cent chance of living to 90 or longer. Yet the financial plans of many individuals will not reflect these averages.

"You have to watch longevity risk," says Chris Derbyshire, chief investment officer at Seven Investment Management. Planning for his own retirement, the 50-year-old came up with a financial model to gauge how his investments would perform over time. He initially assumed an "end point" of 85 years — until he completed a free online life expectancy test. Faced with a potential investment window of 45 years, he then examined the impact of delaying the moment at which he started taking an income from his investments.

"I've probably got 10-15 years of compounding before I hit retirement and have to begin spending the money," he says. "But if you can live relatively frugally around retirement, that makes a big difference to the outcomes as compounding works best when your pot is large."

These kinds of mathematical equations are complicated by how long we might stay healthy. Public Health England says boys born between 2013 and 2015 have an average "healthy life expectancy" of just over 63 years, and can then expect to spend an average 16 years in poor health. Girls will on average be healthy until just over 64 years, and then spend 16.1 years in poor health.

The average "life expectancy gap" between the highest and lowest earners in the UK is nine years. However, the gap in the "healthy life expectancy" is 19 years. So while the wealthiest can expect to live for longer, many of those extra years may require expensive social or residential care.

Pension pressures

Pension freedoms introduced in 2015 have increased worries that people will run out of money in old age. The number of people opting to keep their funds in drawdown has overtaken those choosing to buy guaranteed income via an annuity. Now that people can access pension savings from the age of 55, there are fears that retirement funds could be spent too early.

The over-85 age group is now the fastest growing segment of the UK population, prompting the FCA to prepare a strategy on the ageing population. The watchdog stressed the importance of "deepening our understanding about how markets work for older consumers". One recommendation was that the government could introduce a mid-retirement financial health check to prompt people at 75 to reconsider their financial position and plan for the remainder of their lives.

Prof Scott says we cannot afford to take our pensions at the age we currently do. As we are ageing more slowly, he says we should factor in being able to work and pay into a pension for longer. He predicts those currently aged 45 will probably work until 75, and that 20-year-olds will probably work until they are 80.

Ideally, we should opt for a series of careers with breaks between them for mid- and late-life training. We should all plan to fund our housing and think about paying for "extreme old-age care", he says, adding that many of the financial products currently on the market are not up to the job.

While annuities guarantee a fixed or inflation-proofed income, rates are at all-time lows. Once taken, annuity rates will not increase when interest rates rise. This has encouraged some people reaching retirement age to opt for drawdown, with the intention of buying an annuity later. Despite rising longevity, the average age at which an annuity is purchased is 62 — the same as it was at the turn of the century.

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