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Green Paper on Demographic Change
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14 October 2005

Dear Sir,

Norwich Union Life welcomes the opportunity to comment on the Commission's Green Paper on Demographic Change. I enclose a copy of our response to the Paper, which I hope you will find an interesting contribution to the debate.

Should you wish to discuss any of the points we raise further, please do not hesitate to call me.

Yours sincerely

Richard Cox
Public Affairs Manager
Norwich Union Life

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# Norwich Union Life's response to the European Commission's consultation on the Green Paper on Demographic Change

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## 1 Key points

- The fact that we are on average living longer is good news. However, this inevitably presents a huge challenge to the future structure and funding of social care systems.

- The issues can be addressed by a number of complementary strategies co-ordinated across the EU. It is likely this would include a combination of:
  - Working later in life
  - Saving more money to fund a longer retirement
  - Increasing state contributions to social care and pensions systems
  - Increasing the productivity of the working population.

- The challenge of an increased dependency ratio is compounded by the fact that people are saving less money (as a proportion of their income) towards their retirement.

- The private sector has a critical role to play in reversing this trend and thereby ensuring that tomorrow's elderly generations are less reliant on tomorrow's working population.

- Norwich Union recognises its role in increasing levels of private savings and pensions, coupled with seeking to better understand, and address, the underlying reasons why people are not saving as much as is needed.

- We would urge caution around over-reliance on increased fertility as a panacea. Whilst this may fill a gap in the short term, it may cause further problems in the long term.

- A more sustainable strategy would be to focus on increasing investment in education, skills and technology to ensure we make the available resources more productive, rather than making more resource available.

It has been encouraging to witness the debate on demography and ageing moving up the EU agenda. The Commission Green Paper on Demographic Change rightly recognises that demographic change has significant social, economic and political implications for all nations across Europe. Norwich Union are pleased to be able to contribute to a much needed debate on one of the major challenges facing our generation – not to mention the next.

It is right that an issue with such far-reaching implications across all member states, particularly due to increasing migration within the EU, is discussed at EU level. We feel every effort should be made to ensure that experiences and possible solutions are shared between member states - there is therefore a policy co-ordination role for the Commission. However, member states retain responsibility for delivering policy responses which reflects the individual characteristics of their respective population.

As a major financial services provider, Norwich Union initially approached this debate from the perspective of how people are going to fund what could be an extra ten or 15 years in retirement, and how a declining number of the working population will support a growing number of non-working retirees. These are clearly significant economic challenges on their own but we recognise, through engagement with other contributors to the debate, that there is a much wider agenda including employment and social issues such as diversity in the workplace and barriers to fertility.

In recognition of the complex interaction of social, employment and economic factors, we believe that successful discussions would benefit from a horizontal approach involving and engaging all relevant Directorates-General within the Commission. Indeed we feel the Commission should give consideration to establishing a high level cross-Directorate-General group on ageing to draw together the best ideas from all areas and start to develop consensus around the most effective approach.

Having said that, progress demands an initial stimulus and Norwich Union welcomes this initiative from the Directorate-General Employment, Social Affairs and Equal Opportunities as an essential first step. We are pleased to have the opportunity to provide our views and develop a dialogue with the Commission at this early stage.

## 3 General observations

Having considered the various issues relating to fertility raised in the Green Paper and at the Demography conference in July, it appears that there are essentially two facets to the debate which, whilst inter-related, we feel should be considered quite separately. Firstly, it has been identified that people are not having as many children as they would like and secondly, there is an imbalance between older 'non-workers' and younger 'workers' (an increasing dependency ratio). The challenge to enable people to have as many children as they would like appears to be mainly a social challenge whereas the challenge of an increasing dependency ratio presents an economic challenge – exacerbated by underfunding in private retirement provision.

We feel that whilst increasing fertility in order to address an increasing dependency ratio may seem an obvious response it does not seem a sustainable solution over the longer term. In the short to medium term, increasing fertility would indeed worsen the dependency ratio as children are just as dependent on the working population as the elderly. This would cause most strain if there were to be a larger generation of children to support just as the major impact of the dependency ratio hits home between 2030 and 2040 when the post war 'baby boomers' reach retirement. Even if fertility rates were significantly increased from tomorrow, perhaps stimulated by increased tax incentives and child care provision, the new generation would reach productive age too late to have a major impact on economic growth and government revenue required to pay the pensions of the 'baby boomers'.

Moreover, children born today may help provide for pensioners in 30 or 40 years time, but in 60 or 70 years time they too will require support. Any increase in fertility rates would have to be sustained indefinitely or the problem of an increased dependency rate will merely be delayed. It is right that people should not be prevented from having as many children as they can support (or want) but it is misleading to present this 'social right' as a sustainable solution to the demographic challenge of an ageing population.

We feel that it would be more productive to focus attention on ways to encourage the current working population to save more for their retirement, alongside initiatives to tap into the productive capacity of older people. Increasing personal savings and unleashing this capacity will allow future older generations to contribute themselves to the economic challenges of the growing dependency ratio which their good fortune in living longer is generating.

An ageing population also influences the productive capacity of a nation's savings. A higher proportion of people in old age means a lower proportion of wealth invested for growth - as people get older, they invest more in bonds and other lower risk assets, rather than equities, and this removes a proportion of productive capital from the economy. This is exacerbated by the compulsory requirement to buy an annuity, which means people are locked into investments in bonds and cash for up to 30 years, rather than higher risk equities which can boost innovation and economic growth, thereby leading to greater national and EU wide income. The requirement for the UK's stakeholder products to be 'lifestyled' (moving into less risky assets as the customer approaches retirement) also contributes to this issue.

Older people have a lifetime of experience and a huge amount to offer the workplace. Norwich Union welcomes the measures taken through the implementation of the Age Discrimination Directive next year to prevent older people being forced to stop working before they might like to. However, we would also encourage the Commission to investigate further why most people do not want to work beyond 60 – the research outlined below was commissioned to explore attitudes to ageing and working later in life.

## 4 Active ageing

In the UK, Norwich Union is actively supporting key aspects of the Department for Work and Pensions (DWP) Informed Choice programme, which aims to remove the cliff edge which confronts too many people between their working life and retirement. Like the DWP, we believe it is important to identify opportunities for people to continue working, whether that be full time, part time or on a voluntary basis.

From the perspective of a large employer, Norwich Union Life's diversity strategy includes a focus on older workers. Ensuring our workforce reflects our customer base will help us to get closer to these customers and the potential opportunities that this brings. Our average customer age is 50 so focus groups have been organised with our employees over this age to better understand how we can attract and retain staff from this age group. For example, the company recently reviewed its recruitment adverts to ensure they would not be seen as discriminatory - research indicates many workers over 50 are put off applying for jobs early in the process due to perceived or implied discrimination in job adverts.

Ensuring older workers have skills relevant to a modern labour market is essential if they are to continue working through their 50s and 60s. Employers should encourage a culture of lifelong learning throughout peoples' careers so that employees can achieve their full potential and take advantage of any opportunities regardless of their age or stage in their career. This should be coupled with a phased programme of advice and support from employers as individuals approach their retirement age to avoid the current experience where many people are offered advice only in the months before their official retirement date. Working with employees at an early stage, perhaps one, two or even five years ahead of retirement, would enable employers and employees to identify any skills and training needs ahead of time. This planned approach will enable employees to either continue in their current role or possibly change the direction of their career entirely - encouraging and enabling them to stay in work for longer.

### 4.1 Attitudes to retirement research

*Norwich Union commissioned research, conducted by market research company ICM, to further investigate retirement age and working later in the UK and understand how working later in life can play its part in helping fund future pensions provision. The quantitative part of the research sampled 1,000 adults aged between 18 and 70 (non-retired) in August 2005. In addition, qualitative research consisting of 6 focus groups of people aged 45 – 55 working, 55 – 65 working, 60 – 70 semi – retired & retired were carried out. The key findings of this research are as follows:*

- 46% expect to retire before state pension age, though this reduces to 29% in the 55-64 age group - 22% expect to retire at state pensions age, 27% after.
- Of those who plan to retire after state pension age, key reasons given are:
  - It is my choice when I retire – 81%
  - I enjoy the social interaction at work – 74%
  - I enjoy the mental stimulation – 74%
  - I will need the extra income in order to enjoy a comfortable retirement – 69%
  - I want to work past state pension age but only part-time – 64%
- 85% of those surveyed accepted the fact that life expectancy is rising and the average length of retirement has increased. However, only 52% accepted the view that people must work longer because they will be living longer.

- Health is the biggest perceived barrier to working past the state pension age (23%)
- 27% of those in work felt they would be prevented from working as long as they would like.
- 64% of those who felt they would be prevented from working as long as they would like linked this to employment related issues:
    - compulsory retirement age at work (20%)
    - employer culture not supporting older workers (18%)
    - employer not offering part-time flexibility (16%)
    - no job opportunities for older workers (10%)
- Post-retirement part time work was attractive to many, but only on their own terms and with jobs that offer a challenge, stimulation and structure
- Whilst many hope to live to 90 and some think they will, the uncertainties of health and energy levels in the ageing process makes the decade 60 -70 the safest bet to be able to enjoy a rewarding retirement. The majority of people in this research think 60 is an ideal retirement age.
- 82% of those questioned plan to retire before the state pension age, with men, on average, planning to retire at 60 and women at 59. However, these plans change as people become older – 25-34 year olds plan to retire at age 58, but 55-64 year olds, for who this decision is more relevant, plan to retire at age 63.
- 41% of those who want to retire before the state pension age would be prepared to work beyond it. This is highest amongst younger age groups, gradually decreasing to 29% for 45-54 year olds, and 28% for 55-64 year olds.
- The need to raise the state pension age is viewed as a result of mismanagement by past/present Government, not as a consequence of people living longer.

The Department for Work and Pensions in the UK offer a deferral scheme whereby someone's state pension is increased by 10% if they delay retirement for a year, up to 50% if they defer by five years:

- 78% of respondents were unaware of this scheme, however, once it was explained, 60% of people were influenced by the incentives on offer, and would consider delaying their retirement by a year for extra money.
- Of those who would not be influenced by this, 17% said the basic state pension had no effect on their retirement plans.
- The older people are, the less likely they are to be influenced by this incentive. Those aged 18 to 24 were 70% in favour of delaying claiming their state pension, but only 59% of those aged 45-54 and 52% of those over 65 would be influenced.

The challenge we face is to find appropriate and workable ways to encourage people to either work later in life or make adequate provision for a longer retirement. 41% of those who intended to retire before the state pension age would be prepared to consider working beyond this age.

Further promotion of personal choice, flexible work/life arrangements closer to the retirement age, and new initiatives to put the individual in control of their retirement age, are the obvious starting points.

## 4.2 IPPR research – Raising the effective age of retirement

*Norwich Union Life sponsored research by the UK think tank the Institute for Public Policy Research (IPPR), which looked at how the UK can raise the effective age at which people retire. IPPR analysed literature from a number of countries to establish how they approached this issue, held a working seminar and conducted qualitative research in spring 2005 looking at the expectations of people in the workforce and how they might respond to an increase in the state pension age. Key conclusions:*

- Post-war pension systems were designed to fund somewhere around 15 years of comfortable retirement; at the turn of the century, the average effective length of retirement ranges from 16 to 20 years for men and 21 to 25 years for women.
- People see the years between 65 and 70 as 'protected time' to enjoy a healthy comfortable retirement. After 70, they expect their health to begin to deteriorate.
- The decision when to leave full-time work or "wind down" to part-time employment should be a personal choice rather than being coerced into doing so by government. However the declining generosity of public and private pensions will force people to 'choose' to work longer.
- Employers can no longer afford to fund early retirement and will increasingly need to actively recruit older workers.
- The state pension age should rise to send a clear signal about the desirability of working longer. This can only be sold as part of a package that includes a significant increase in the generosity of the basic state pension.
- Government needs to clearly signal that people working longer on average is an important component of a sustainable pension settlement.
- Any government that raises the state pension age will be undertaking a significant political risk.
- The political challenge for the government is to try and sell a deal whereby a significantly enhanced basic state pension is linked to receiving that pension later in life for workers reaching 67 by around 2030.

It is important to acknowledge that the challenges presented by an ageing population extend to long term care as well as pensions provision.

Figures from the UK's Government Actuary's Department indicate that life expectancy has increased at a faster rate than healthy life expectancy, meaning that on average, people are spending longer in ill health in later life. For example, each year in the UK over 90,000 people over retirement age suffer a first stroke, and 37% of those aged 65-74 and 47% of those over 75 say they have a long-standing illness which limits their lifestyle.

The challenge then is to construct systems which support both the provision of income in retirement and the provision of care. Historically this topic has not been given the same attention as the issues around pensions but has very similar social, political and economic implications and should therefore not be ignored.

The economic pressure on the working generations will increase not just because of the need to provide pensions, but also to provide long term care. The UK Government Actuary projects that the number of care home residents will triple between 2004 and 2051 to 1.2million, with 80% of long term care costs being met publicly - state spending on long term care is expected to reach 1.5% GDP by this time.

Norwich Union offers an Immediate Care Plan for those in retirement who need immediate finances to provide for long term care. Once a single premium (over £5000) is paid, we guarantee (dependent upon factors such as sex, age, health and interest rates) a regular benefit payment for the rest of their lives. Government policy currently provides funding for those in care homes receiving nursing care, though there is a shift away from care homes to community - and home-delivered care. Private protection plans such as Norwich Union's can provide more than the state and can help in sharing the risk of care provision costs between the individual and the state.

## 6 Attitudes to saving for retirement

*In November 2004, Norwich Union commissioned consumer research to help understand peoples' attitudes to saving for retirement. Key areas explored were the extent of 'consciously irrational' behaviour of consumers (knowing they should save but taking no action), the impact of debt and wide availability of credit, and understand what role financial providers can play in encouraging people to save for retirement. Headline insights were:*

- In consumers' minds, 'saving' means one of two things – 'not spending' and 'investing'. Many consumers are locked into a short term mindset.
- Uncertainty in the present contributes to a dominant 'live for today' culture. The 'here and now' matters much more than some distant future.
- Where people do think further ahead, what they consider to be a 'long term' time horizon varies dramatically – for example, 3 years for someone in their late twenties, 10 years for someone in their late thirties.
- Multi-career planning, an increase in self-employment, job instability and fear of redundancy can make consumers think that pensions are not relevant to them. There is a perception of pensions as fixed, rigid, inflexible and old fashioned.
- Credit and debt are replacing and eroding saving in the attitudes and behaviours of many consumers who now think in terms of short, medium and long term debt, rather than saving, as a form of financial planning.
- Credit and debt are facilitating a lifestyle for consumers that is often at odds with actual income – creating a subliminal message that you do not need to save in order to live the lifestyle that you want (especially the case in the 18-25 age group, but also spilling into other life stages).
- Increasingly, consumers see investment in property as a viable alternative to a pension - this attitude operates across all life stages and is increasingly translating into behaviour (buying property in the UK and abroad). Older consumers (45+) are increasingly becoming advocates of property investment to younger people.
- Despite a lack of willingness to 'give up' on pensions in principle, consumers will and are giving up on pensions in practice because property is seen to offer an easier, more secure return on investment.
- 'Pensions' creates an immediate disconnection for consumers due to a range of negative associations which do not align with their desire for a hopeful and optimistic future.

There have been huge changes in the marketplace in recent years such as the growth in popularity of pensions as a means of funding retirement, the accessibility of credit, and stock market falls which contributed to poor product performance, such as endowments. This has contributed to a decline in consumer confidence which is discouraging people from saving for retirement.

Attention needs to focus on how to rebuild trust in saving for retirement. In the UK, the industry has already taken steps to improve its reputation alongside initiatives to reinvent the culture of long term saving amongst the population such as improving customer communications and a drive to deliver greater transparency.

A lifecycle of products

As customers, markets and regulations evolve, Norwich Union recognises that we need to alter our business to respond to consumers' changing needs:

| Age | Traditional life cycle | Emerging life cycle |
|---|---|---|
| **20s - early 30s** | **Financial independence**<br>Stable employment, income rising, cash rich, then family pressures | **Financial responsibility**<br>Expenditure outweighs income |
| **30s - mid 40s** | **Financial freedom**<br>Income & expenditure stabilise. Expenditure still high due to children. | **Financial fluctuations**<br>Due to job changes, redundancy and relocations. |
| **Mid 40s - mid 50s** | **Financial freedom**<br>Children leave home, sharp fall in expenditure. Income constant. | **Financial injection**<br>Children leave home. Redundancy, early retirement. Possible inheritance. |
| **Mid 50's - mid 60s** | **Financial prosperity**<br>A short period of high disposable income. | **Financial uncertainty**<br>Income fluctuates then falls sharply and remains constant. Elderly care for relatives. |
| **Mid 60s and beyond** | **Financial survival**<br>Sharp fall in income due to retirement. Fall in living standards. | **Financial deficiency**<br>Expenditure falls as older relatives die then rises as care required for themselves. |

The above table reflects how life stages are becoming more flexible but it must also be noted that individuals no longer fall into neatly labelled boxes and therefore market segments are less easily defined than in the past. Norwich Union has adapted its approach to consumers to reflect the more fluid life stages along the lines of the table above. We have developed a customer segmentation model to allow us to target products and marketing to people according to their position relevant to these key life stages. Broadly, these can be defined as:

- Non-family: singles and couples under 45 without children
- Family: anybody with dependent children (under 18)
- Pre-retired: those aged 45 – retired, without children, or singles and couples with children over 18
- Retired: those adults who have left work and are decumulating assets from the savings, investments and pensions they have built up over their lifetime

Many of our products are suitable for customers in different life stages, for example, our protection and investment products are popular with those in all segments, whereas pensions are the most popular product type with those in the family and pre-retired segments. We also provide products specific to certain groups, such as equity release and annuity products for the retired. Increasingly, many of our products are flexible to allow people to move products as they move though life stages, for example offering a choice of funds which reflect the different attitudes to risk which may evolve as peoples' circumstances change.

## 7 About Norwich Union Life

- Norwich Union is part of the pan-European Aviva group. which is the world's sixth largest insurer, with 30 million customers and businesses in 15 EU member states[1].
- Norwich Union is the largest insurer in the United Kingdom, with a market share of 12% in the life sector.
- Key facts and figures on Norwich Union:
  - UK's largest provider of life, pensions and investment products, with a market share of around 12%.
  - Extensive range of products covering pensions, savings and investments, life assurance, critical illness, equity release and healthcare insurance.
  - Around 12,000 employees in the UK, and nearly 7 million customers.
  - Product distribution channels: direct sales, Independent Financial Advisers (IFAs), Building Societies, Tesco Personal Finance and a joint venture with the Royal Bank of Scotland.
  - Independent market research shows Norwich Union to be one of the most trusted long-term savings brands in the UK.

## 8 Contact details

For further information or to discuss any of the points raised in the response from Norwich Union please contact:

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[1] Key brands include Aviva, Norwich Union, RAC, Morley Fund Management, Hibernian, Delta Lloyd and Commercial Union Poland.

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