

"NO-ONE KNOWS HOW THE WORLD WILL LOOK IN 50 YEARS' TIME."

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GOVERNMENT'S LONG-TERM FINANCIAL PLANNING

Maintaining sound public finances is one of the Treasury's key Strategic Objectives.

The UK economy faces a number of strategic challenges, including an ageing population, climate change, and globalisation. These challenges have long-term implications for the public finances, for example:

- > an ageing population may lead to increased public expenditure on health or pensions
- > globalisation may impact on the size of the UK economy, which in turn would affect revenues.

The Government launched the Long-term public finance report in 2002 to provide analysis of long-term developments and their potential impact on the public finances. The latest report was published in December 2009 alongside the Pre-Budget Report. It contains projections of public expenditure over the next 50 years across a range of areas, including many of actuarial interest such as:

- > STATE PENSIONS
- > PUBLIC SERVICE PENSIONS
- > HEALTH
- > LONG-TERM CARE

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GAD is naturally well placed to assist with such long-term financial planning and, in particular, plays a key role in projections of state pensions and public sector pensions.

STATE PENSIONS

State pensions, along with other benefits such as those paid on incapacity, bereavement and unemployment, are paid out of the National Insurance Fund. The Government Actuary reviews the operation of the National Insurance Fund at least every five years. This review considers the Fund's long-term financial position, taking account of the projected benefits to be paid and the National Insurance contributions to be received in the future. The latest review is due out this spring.

PUBLIC SERVICE PENSIONS

The Government Actuary is also involved in projections of public service pensions. There are 7½ million members in Pay-As-You-Go (or unfunded) public service pension schemes, including teachers, NHS workers, civil servants, the armed forces, police officers and fire-fighters, all with different pension schemes. This means producing projections of the pension expenditure is challenging. We need to ensure that our models are sophisticated enough to be reliable but simple enough to provide timely results.

The National Audit Office has drawn significantly on GAD's projections in their [recent report](#) on the cost of public sector pensions. This report will help to inform the public debate about the affordability of public service pensions. The National Audit Office also intends to publish a second report later this year examining the recent changes in these pension schemes. These changes include the Government's 'Cap and Share' policy.

CAP AND SHARE

It was agreed that public service pension schemes would introduce 'Cap and Share', following the agreement to introduce a Normal Pension Age of 65 for new entrants to the civil service, NHS and teachers' pension schemes. Cap and Share involves sharing increases in the cost of pension provision, such as improving longevity, between employers and employees up to an agreed employer contribution cap, beyond which further increases are the responsibility of employees. Any increased costs that fall to employees would result in either increased employee contributions or reduced benefits for future service or both. The cost of each scheme's provision will be assessed through the periodic scheme valuations that take place every 3 or 4 years.

The latest Long-term public finance report projections included allowance for 'Cap and Share' for the first time. This meant we had to consider the potential results of the schemes' future valuations. Providing an indication of the result of a valuation due next month or next year is not unusual, but doing the same for valuations due in 50 years' time is.

RECOGNISING UNCERTAINTY

Of course, no-one knows how the world will look in 50 years' time, and no one possible view of the future will give the full picture. Both the review of the National Insurance Fund and the Long-term public finance report include projections for several different scenarios to illustrate and help to quantify the uncertainties.

For example, there have been significant improvements in life expectancy over the last century and the most recent data has shown faster rates of improvement than in the past. However there is no consensus among academics or actuaries on whether rates of improvement will stay the same, increase further or tail off. GAD provides projections based on higher and lower future life expectancies to illustrate the financial impact of these possible outcomes.

So although we do not know how the world will look in 50 years' time, we can consider a range of ways it might look to assess the potential impact of changes in demographics, and economic activity, on the public finances.

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HOW LONG IS THE LONG TERM?

For many organisations long-term financial planning would mean the next 5 years, not the next 50, but the Government is conscious of the long-term nature of its financial commitments. GAD has actuaries with experience across a wide range of fields who are proficient in finding innovative ways to help the Government's long-term financial planning.