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DC & AUTO-ENROLMENT

Pensions: The great inflation divide

By Samantha Downes | July 3, 2023

Savers with an inflation-protected pension scheme will be £1,500 better off by April 2024 than those with capped inflation protection, investment platform ii has warned.

Retail investment platform interactive investor, claimed some pensioners were much more protected than others when it comes to inflation, and those in an inflation-protected pension scheme would be £1,500 better off by April 2024 than those with capped inflation protection.

Some pension schemes, including four of the main public sectors pensions - **Teachers**, NHS, armed forces and local government - were inflation-linked and uprated each April based on **CPI inflation** in the previous year.

These pensions increased by 10.1 per cent this April, in line with the increase in the state pension, protecting pension savers and pensioners from inflation.

In contrast, private sector final salary pension schemes often have capped yearly increases, meaning that pensioners' incomes will only rise by a maximum of around five per cent each year. Pensioners with these schemes lose out in times of high inflation, interactive investor said.

Amount of pension among different pensioner groups:

Year:	22/23	23/24	24/25
Inflation:		10.1%	7%
<i>State pension only:</i>	£9,628	£10,600	£11,342
<i>Inflation-linked final salary</i>			
<i>pension plus state pension:</i>	£29,628	£32,620	£34,903
<i>Capped final salary pension</i>			
<i>plus state pension (5% cap):</i>	£29,628	£31,600	£33,392
<i>Defined contribution pension</i>			
<i>plus state pension:</i>	£26,025	£27,817	£29,420

Source: interactive investor - assumptions: final salary calculation assume pension income of £20,000 in 22/23, inflation of 7 per cent based on Bank of England May forecast for Q3 2023

Alice Guy, head of pensions and savings, interactive investor said there were four distinct groups of pensioners: those relying solely on the state pension; those with pension pots, relying on investment performance; those with a final or average salary pension, often rising at a maximum of five per cent per year and the luckiest of all - those with an inflation-linked final or average salary pension.

She said a huge gulf was opening up between those with inflation linked pensions and those with a capped pension increase, often five per cent, a gap that would only widen the longer high inflation continues.

Guy added: "Most companies closed final salary pension schemes to new members during the 1990s and early 2000s, instead offering defined contribution pensions where individual employees invest in their own pension pot. This group can still achieve a comfortable retirement if they regularly invest over the long term in a balanced portfolio, but they're unlikely to beat the gold-plated returns of those with a final or average salary pension."

"There's a myth that all pensioners are rich, but that's simply not true. Many retirees have no workplace pension at all, relying solely on the state pension. Auto-enrolment rules came into force in 2012, and before that date many smaller employers didn't offer a workplace pension. It was possible to work for your whole working life and have nothing to show for it, apart from the state pension."

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