# Towards a new age:

## The future of the UK welfare state

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The International Longevity Centre – UK (ILC-UK) is an independent, non-partisan think tank dedicated to addressing issues of longevity, ageing and population change. It develops ideas, undertakes research and creates a forum for debate.

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# Foreword

## Baroness Sally Greengross

In 1942, William Beveridge laid out his plans for a new social contract which would lead to the birth of the UK welfare state. After observing considerable destitution amongst large swathes of the population, Beveridge set out an ambitious programme for reform which included universal healthcare, protection for the unemployed, pensions for older people and better housing conditions.

Out of the embers of the Second World War, the welfare state was born and it coincided with a prolonged period of economic growth – not just at home, but right across Europe, the United States and parts of Asia too. It was supported by rapid growth in working age populations around the world. As economies grew, poverty rates fell, household incomes rose and life expectancy surpassed the expectations of the very best analysts, again and again and again.

It is over 70 years since Beveridge. Like many other developed nations, the UK has capitalized on its demographic dividend – a period of rapid growth in the working age population - and now faces a significant rise in the older population. While ageing is a sign of great social and economic progress and should be celebrated, it also poses a threat to the sustainability of welfare systems – not just in the UK but around the world. An increasingly sizeable older population may require larger public outlays to meet pension and healthcare commitments, but with growth in the working age population stagnant or shrinking, such commitments may be difficult to sustain. We need a new Beveridge which takes into account demographic shifts in a way that is fair across social groups and different generations.

Understanding the financial challenges posed by ageing is one thing, developing solutions and coping strategies is another. Not only will reform efforts need to identify a set of measures that are economically efficient and fair across groups, but they will also need to be able to garner sufficient political support to enable and legitimise their implementation. The welfare state is a sensitive issue, tampering with it can create public and political upheaval. For this reason, we need an open and honest national debate about the future of the welfare state which transcends party politics.

Our hope is that this volume of essays can help kick-start the conversation. In

this regard, we are extremely grateful for such high quality contributions from a wide range of experts in different fields including; academics, politicians, former ministers and economists in order to explore potential challenges and possible solutions. The scope of this volume is necessarily broad and ambitious, but it is only by encouraging thinking and debate of this sort that we will be able to address the challenges that lie ahead.

# Biographies

**Ben Franklin:** Head of Economics of Ageing at the International Longevity Centre UK.

**Dr. Cesira Urzi Brancati:** Research Fellow at the International Longevity Centre UK.

**Professor Nicholas Barr:** Professor of Public Economics at the London School of Economics.

**George Magnus:** Former Chief Economist and Senior Economic Adviser at UBS Investment Bank.

**Lord David Willetts:** Executive Chairman of the Resolution Foundation and former Minister for Universities and Science.

**Norma Cohen:** Former Demography Correspondent at the Financial Times and currently a PhD candidate at Queen Mary University of London (QMUL).

**Professor Elsa Fornero:** Professor of economics at the University of Turin, and former Italian Minister for Labor, Social Policies and Gender Equality.

**Steve Webb:** Director of Policy and External Communications at Royal London and former Minister of State for Pensions.

**Gregg McClymont:** Head of Retirement Savings at Aberdeen Asset Management and former Shadow Minister for Pensions.

**Andy Tarrant:** Head of Policy at the People's Pension.

**Professor David Bell:** Professor of Economics at the University of Stirling.

**Professor Danny Blanchflower:** Professor of Economics at Dartmouth University.

**John Philpott:** Director of The Jobs Economist.

**Professor Chris Husbands:** Vice-Chancellor of Sheffield Hallam University and former Director of the Institute of Education, University of London.

**Anthony Seldon:** Vice-Chancellor of The University of Buckingham.

**Phil Hope:** Former Minister of State for Care Services, Director of Hope Consultancy, and Visiting Professor at Imperial College.

**Sally-Marie Bamford:** Director of Research and Strategy at the International Longevity Centre UK

**Kieran Brett**: Director of Health at iMPOWER and former Special Advisor to the Secretary of State for Health

**Sir Michael Lyons:** is non-executive chairman of the English Cities Fund and Participle Ltd; and author of the Lyons Housing review.

**Caroline Green:** Assistant Chief Executive Oxford City Council and worked on the Lyons Review.

**Neal Hudson:** Associate Director of Savills Residential Research and worked on the Lyons Review.

**Lord Richard Best:** Member of the House of Lords, Former Chief Executive at the Joseph Rowntree Foundation and National Housing Federation.

**Professor Danny Dorling:** Halford Mackinder Professor of Geography at the University of Oxford.

**Nusrat Ghani MP:** Chair of the All-Party Parliamentary Group on Ageing and Older People and MP for Wealden.

## Acknowledgements

We would like to thank all the authors for excellent contributions. They wrote to a tight deadline, and responded to our comments as well as embracing our invitation to think about solutions as well as problems. We would also like to thank Munich Re for sponsoring ILC-UK's research for this project. Finally, the editors would like to thank all our colleagues at the ILC-UK for helpful input throughout the process.

# Introduction

## Why now? The need for a debate on the future of the welfare state

Population ageing is likely to have profound implications for us all. At the International Longevity Centre, we are concerned with understanding what these implications might be and how best to mobilise public policy, industry endeavour and individual action in order to make the most of the opportunities as well as to mitigate the risks. Insofar as ageing poses a challenge, we think it important to understand its different dimensions through collaborative, multidisciplinary research and analysis.

In this context,this book attempts to explore two of the biggest questions of our time:

- How might population ageing impact on the wide array of policies and institutions we call the UK welfare state?
- What reforms to the welfare state might be necessary in order to ensure long run sustainability and maximise wellbeing?

The past 30 years have been punctuated by occasional articles and debates about the so called "crisis of the welfare state". Threats to the state are typically believed to emanate from two sources: globalisation and population ageing.

On the one hand, globalisation is deemed to pose a risk to the welfare state by inducing a race to the bottom on taxation in order to attract business investment at the expense of social spending. But such a future is not inevitable : globalisation can actually play an important role in sustaining the welfare state by supporting economic growth, while social policy decisions are at the very least tempered by a government's desire to secure support from the electorates they serve[1].

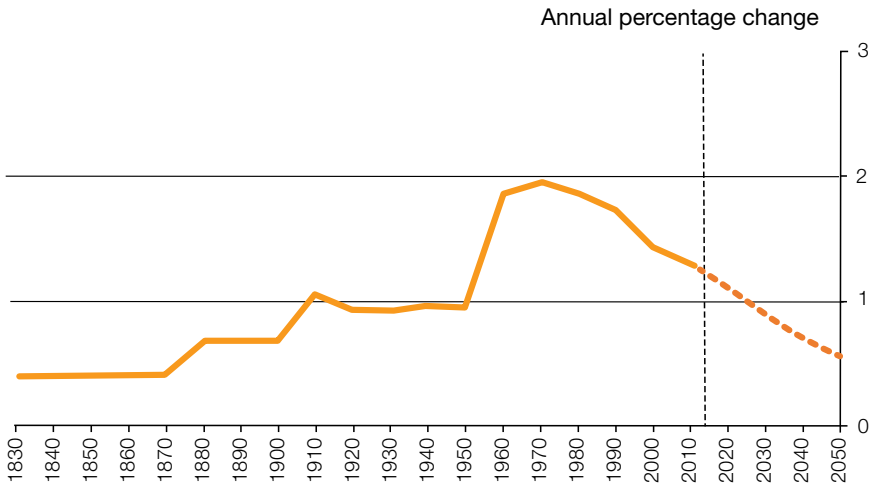
Demographic change on the other hand, is deemed to pose a risk to the welfare state by reducing the number of workers relative to the number of non-workers thereby implying either increased tax burdens on the working population or a reduction in welfare spending per head. But such a future is also not inevitable – the average age of leaving the labour force might extend way beyond 70, while technological change may drive up the productivity of the workforce in ways that Keynes first envisaged over 80 years ago.

[1]Trevitt, V. (2009) "The Importance of the Welfare State Under Globalisation" Compass, Think Pieces, No.53

Today these arguments appear more relevant than ever. It is now eight years since the Great Recession and there is a growing realisation that we have entered a new phase in our development characterised by ageing societies, lower global growth and stagnating living standards. Yet in a complex, globalised world, where people and capital can move across borders, it is almost impossible to understand how best to manage the transition to older societies at a local, national and global level.

In this regard, this book focuses specifically on the ageing component of the challenge and how the UK welfare state can respond. Our view is that we are not yet in the midst of a crisis but that unless we properly understand the challenges posed by ageing and consider the potential solutions, we are heading in that direction. Simply hoping that longer working lives or technological change will be sufficient to address the challenge of ageing is equivalent to burying ones' head in the sand. Unlike the 1970s and 1980s when much of the developed and developing world was banking its demographic dividend and experiencing bumper GDP growth, today we stand on the precipice of a new demographic and economic reality. Not only is the UK ageing but so is the rest of the world, and at a significant pace (see chart). This is the future, it will shape us profoundly, and we must adapt in order to make the most of it.

**Global population growth[2]**




Source: United Nations population projections (http://esa.un.org/wpp/) for 1950 onwards; the Maddison-Project (http://www.ggdc.net/maddisom/maddison-projects/home.htm) prior to 1950.

[2] This is a reproduced version of a chart originally produced for Haldane (2015) Growing, Fast and Slow, Speech at the University of East Anglia http://www.bankofengland.co.uk/publications/Documents/speeches/2015/speech797.pdf

## The role and structure of this book

Against this background, we invited a number of experts across different fields to assess the challenges posed by ageing for the UK welfare state as well as the possible solutions. We do not claim to have all the answers, but it is our hope that this volume can act as a catalyst for a proper national debate about how we can reasonably deliver a social contract that is both fair to different social groups and generations as well as being sustainable in the long run. We would hope that most readers would use the book as a point of reference for consultation; and so the chapters have been written so that they can be read in any order, separately or in groups. It is structured as follows:

- **Part 1 explores the background and context for the book.** It includes a provocation by the ILC-UK which argues that population ageing, the welfare state and democracy might be incompatible, together with some headline findings from the new ILC-UK Welfare State Effectiveness Index published alongside this volume.

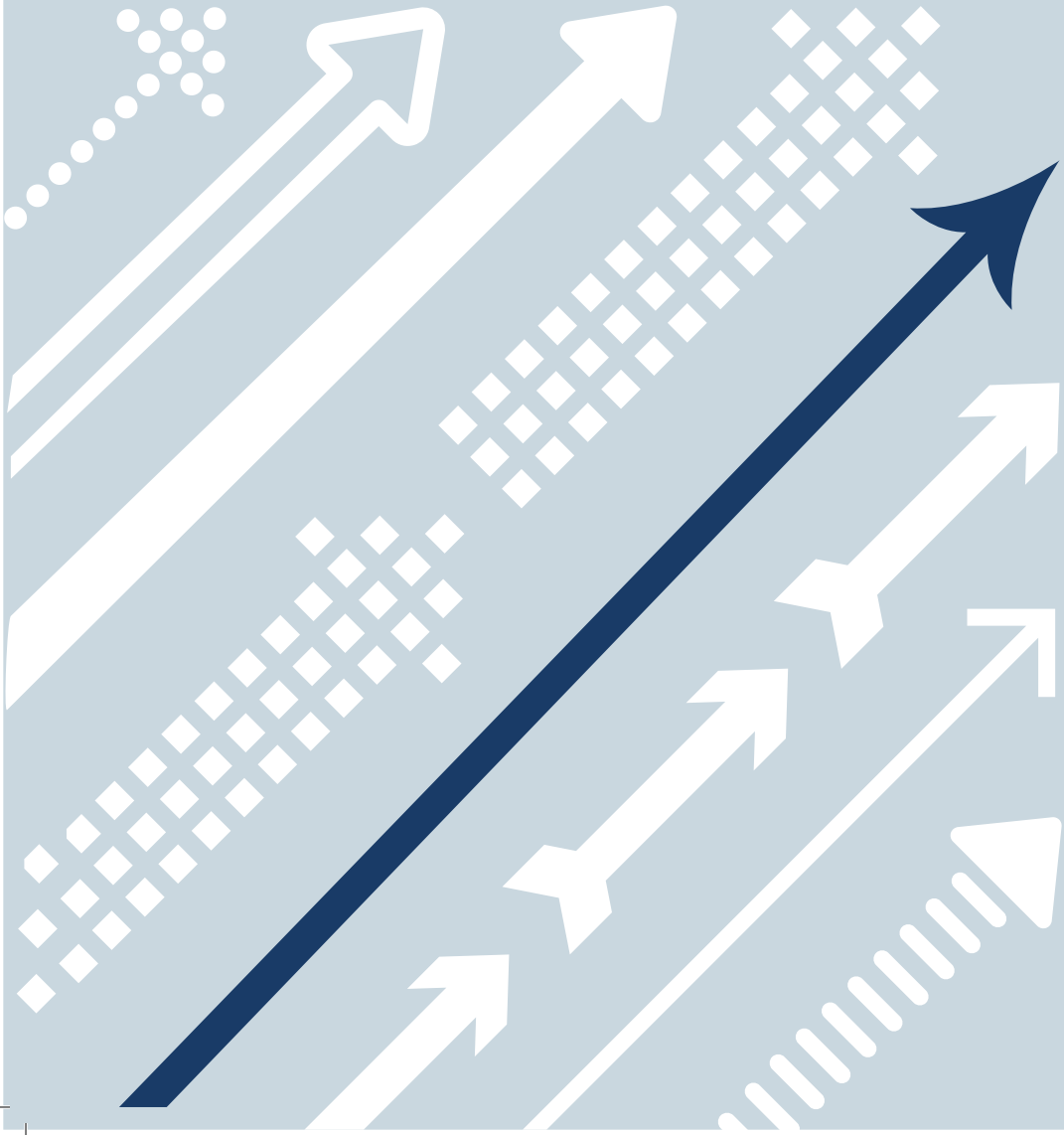
- **Part 2 outlines the challenges posed by ageing for the welfare state**. It includes contributions about the continuing role of the welfare state, how ageing might affect economic growth and intergenerational fairness and the extent to which benefits and entitlements might need to change in order to support future sustainability.

- **Part 3 focuses on solutions or "coping mechanisms" in the face of demographic change.** It is divided into five subsections:
  - **Section 1 explores options for pensions reform**. It includes contributions on the importance of financial literacy to secure the best outcomes from pension reform, a discussion of recent UK pension reform initiatives and an exploration of what further changes might need to be made.
  - **Section 2 outlines labour market challenges and reform options**. It details the labour market issues facing younger people and their long run implications together with a discussion of how we might better facilitate full employment.
  - **Section 3 hones in on education reform**. It includes contributions about the importance of positioning education as a social good, together with a vision of what the future delivery of education could look like if the sector fully embraces new technology.

- **Section 4 explores the future of health reform**. It focuses on the importance of better integration of health, social and community care and the importance of prevention for future sustainability.
- **Section 5 provides recommendations on housing reform**. In particular, contributions highlight the importance of increasing the supply of houses for older people in order to free up the chain for the rest of the market.

- **Part 4 concludes the book by focusing on how we could build a political consensus for reform.** The final two contributions explore the conditions that are most conducive to enabling reform and outline some general principles for a national debate on ageing and the welfare state.

# **Part 1:**
# Background and context



# Towards a dystopian future? Population ageing, democracy and the welfare state

Ben Franklin, Head of Economics of Ageing, ILC-UK

***Welfare state***

Noun

*"A system whereby the state undertakes to protect the health and well-being of its citizens, especially those in financial or social need, by means of grants, pensions, and other benefits"*[3].

## Introduction

The development of the modern welfare state - with extensive programmes for social protection, health, housing and education - coincided with the spread of democratic governments around the world. In De la Démocratie en Amérique, political theorist and philosopher Alexis de Tocqueville observed the self-reinforcing relationship between democratic processes and a drive to improve social welfare. He noted, that as a consequence of frequent elections and close linkages between political leaders and the demos, the political process in a democracy, was driven by a strong "thirst for improvement", "feverish excitement" of the whole of society, and an effort "to improve the condition of the poor"[4].

But the development of the welfare state was not simply related to the formation and consolidation of democratic government. Nor is being democratic a pre-requisite for the development of a welfare state. It has been argued, for instance, that the origins of the modern German welfare state, stem from the days of the semi-authoritarian German Empire of the 19th century[5]. Similarly, there are a number of democratic countries with relatively limited social protection coverage – of which India is a good example[6].

Therefore, as well as focussing on the role of democratic processes in

[3] Oxford Dictionaries online: http://www.oxforddictionaries.com/definition/english/welfare-state

[4] Manfred G. Schmidt (2001) "The Democratic Welfare State" The Pontifical Academy of Social Sciences, Vatican City

[5] Hennock, Ernest Peter, (2007), "The Origins of the Welfare State in England and Germany, 1850-1914: Social Policies Compared" New York, Cambridge University Press

[6] Sriivastava. Ravi, (2013) "A Social Protection Floor for India" The International Labour Organisation

supporting welfare state expansion, many also point to the role of economic development, and in particular industrialisation, as an important catalyst. Rapid economic growth after WWII - often termed the "golden age" - enabled governments of all types, to compensate those who lost out during dramatic phases of societal change. This helped to ensure the smooth functioning of society, including limiting the likelihood of governments being overthrown or, in the case of democratic governments, voted out. Democratic governments are more sensitive to this risk than any other form of government because political leaders are explicitly and regularly held to account for their actions by the electorate[7].

Today we are at an impasse. It appears as though the period of state expansion is well and truly over. At the heart of it, is a concern about the future affordability of government spending in an ageing world[8] coupled with a prolonged, maybe even permanent, hangover from the financial crisis. In this context, this essay poses the question, can democratically elected governments make effective social policy reforms to drive renewal of the welfare state, or will the very nature of democratic politics and the modern welfare state they helped nurture, ultimately undermine such efforts?

## Welfare state: a virtuous circle

Theories of welfare state expansion explore the potential for a virtuous circle. Simply put, effective social policies support greater wellbeing and reduced inequality, thereby leading to increased levels of trust and support in the welfare state. In this way, the welfare state can sustain itself and can grow. Certainly the idea that modern welfare states have, generally speaking, helped to support growth and prosperity is not controversial. For instance, it has been argued that welfare states have fulfilled important functions for the "system of capitalist production, for instance the efficient reproduction of manpower, the formation of human capital or the stabilization of demand.[9]" Similarly, Professor Nicholas Barr's contribution to this volume notes that "there are powerful arguments for the welfare state: it addresses major market failures; by sharing risks, it facilitates economic growth; it pursues widely-supported equity objectives; and it contributes to social cohesion".

[7] Brooks, C. and Manza, J., (2008). "Why welfare states persist: the importance of public opinion in democracies". University of Chicago Press.
[8] Razin, A., Sadka, E. and Nam, C.W., (2005). "The decline of the welfare state: demography and globalization". Cambridge, MA: MIT Press.
[9] See for instance; Hagfors, R; Kajanoja, J; Komu, M (2014) The virtuous circle of the welfare state revisited, Working paper, Kela Research Department

There are of course, many competing views about the actual successes of the welfare state, with others arguing that welfare spending has hindered economic growth and wellbeing by undermining the will to work and entrepreneurial spirit.[10] Rather than having an in-depth debate about the past record of the welfare state, this essay starts with the basic assumption that on balance, the UK welfare state has had a net positive effect on wellbeing, including economic growth and social cohesion, and this has contributed towards its legitimacy and expansion.

## Not all social policy is created equal

Governments do not simply choose social policies according to those most in need, or those best suited to supporting long-run economic growth. Welfare transfers "are the outcomes of a government's strategic choices to seek support by rewarding the interest groups critical for the government's survival". There is some empirical support for this notion – academic studies have shown that rather than reducing income inequality, in some instances welfare transfers have actually raised levels of inequality, particularly when they have occurred in non-democratic countries[11]. But such transfers have also increased the chances of governments surviving, at least in the short to medium term.

To some extent, democracies are insulated from these effects because they have to appeal to a broad coalition of voters in order to remain in power, but this does not mean that they are entirely immune. Leaders in a democracy are unlikely to advocate polices that are likely to get them booted out of power in the run up to an election, however economically beneficial they might be in the long run. In this context, the increasing political power of older voters is likely to play an important role in determining social policy choices and outcomes. Population ageing poses a difficult trade-off for elected officials. On the one hand, ageing may require strategies to downsize the generosity of public pensions and other age-related services in order to support long run affordability. On the other hand, ageing will result in an increasingly important older voting block who will support a larger and more generous welfare system for the elderly[12]. Therefore, democratic governments with the goal of maintaining affordability of the welfare state *and* staying in office, may temper their reforms of age-related spending

[10] Moffitt. R (1992) Incentive effects of the US Welfare System: A review, *Journal of Economic Literature*, Vol. 30, No. 1 (March 1992), pp1-61

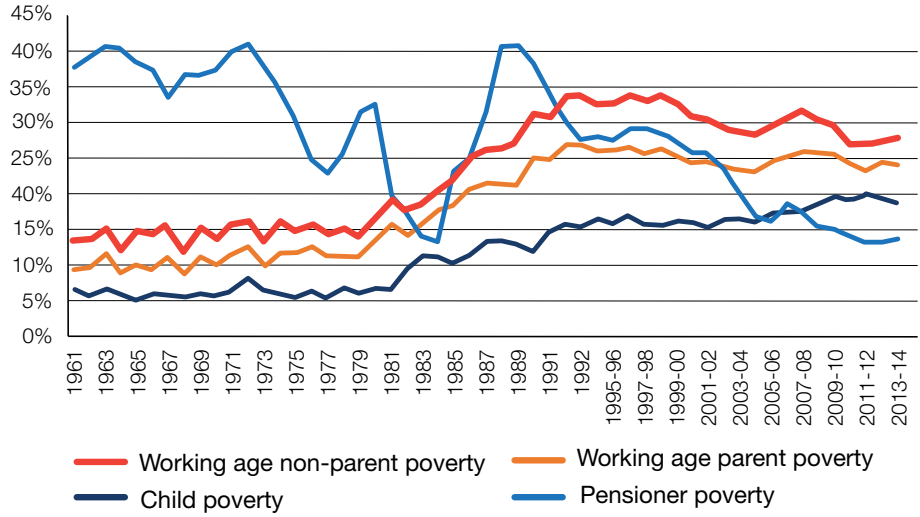
[11] Feng, Y and Gizelis, I (2002) Building Political Consensus and Distributing Resources: A Trade-Off or a Compatible Choice? *Economic Development and Cultural Change*, Vol 51. No. 1 Oct 2002, pp.217-236

[12] Galasso, V and Profeta, P (2007) How does ageing affect the welfare state? European Journal of Political Economy Vol. 23, Issue 2, June 2007, pp. 554–563

but excessively cut back other parts of the system.

In a UK context, such a distortion already appears underway. Between 2010-2015, total spending on pensioners rose by 6.2% in real terms. This rise was both the result of policy change - including and most importantly the triple lock - and population ageing. By contrast, non-pensioner spending fell by 6.5% in real terms driven by policy change (including cuts to tax credits and child benefit) and falling levels of unemployment[13]. While great strides have been made in reducing pensioner poverty over the last decade, we are now in the unprecedented position where a higher proportion of working age people are in poverty than pensioners.

**Pensioner poverty in decline**




Source: ILC-UK analysis of IFS and DWP data. Poverty is defined as less than 60% of median contemporary income

## But older people care for their offspring don't they?

Despite increasing evidence of intergenerational support within a family setting, voters are generally unsupportive of public policy that seeks to address issues of intergenerational inequity at the aggregate level – most notably reforming pay-as-you-go public pensions. Nearly all modern public pension systems rely on substantial transfers of wealth from the working age population to retirees. These systems retain high levels of popular support despite the median voting

[13] Hood, A. and Phillips, D. (2015) Benefit Spending and Reforms: The Coalition Government's Record, *IFS Briefing Note BN160*: http://www.ifs.org.uk/uploads/publications/bns/BN160.pdf

age being below pensionable age. For many observers, this is because of the "disproportionate political capacity of the elderly". But if parents genuinely love their children, why is there not more political will for reform? The answer, it seems, may lie in the belief that within family wealth transfers will adequately compensate children, and that subsequently, by reforming the pensions system and making it redistributive, this will actually penalise their offspring who will have benefited from those same family transfers[14]. As a result, it is possible that parents acting altruistically will seek to protect their entitlement to certain welfare transfers even if this comes at the cost of increasing inequity between generations.

## A downward spiral of welfare state distortion?

As a number of essays in this volume will attest, population ageing is likely to result in reduced economic growth as well as increased expenditure on age-related public spending. While governments may not be able to fully mitigate the adverse economic effects of population ageing, they may, as George Magnus notes in his contribution, be able to develop "coping mechanisms". An effective welfare state may be able to influence both sides of the sustainability equation – impacting on potential economic growth through sharing risks and supporting human capital growth as well as impacting on public spending through expanding or reducing the provision of certain services.

In a world of scarce resources, the choices made by policymakers will be critical. Democratic governments, including in the UK, will have to weigh up the economic and social costs/benefits of undertaking certain reforms against the political costs/benefits. With an increasingly old and powerful voting bloc, which is quite reasonably against reducing the generosity of age-related spending, the chances of aligning effective social policy reform with broad-based political support may fall over time.

But by failing to reform, governments could sow the seeds of the demise of the welfare state. A weakening of the welfare state's capacity to pursue policies aimed at driving economic growth or social cohesion, while continuing to support age-related services at any cost is likely to be unsustainable. At some point, a sudden and severe state retrenchment may be necessary. The UK may have little choice but to redesign the system or face default.

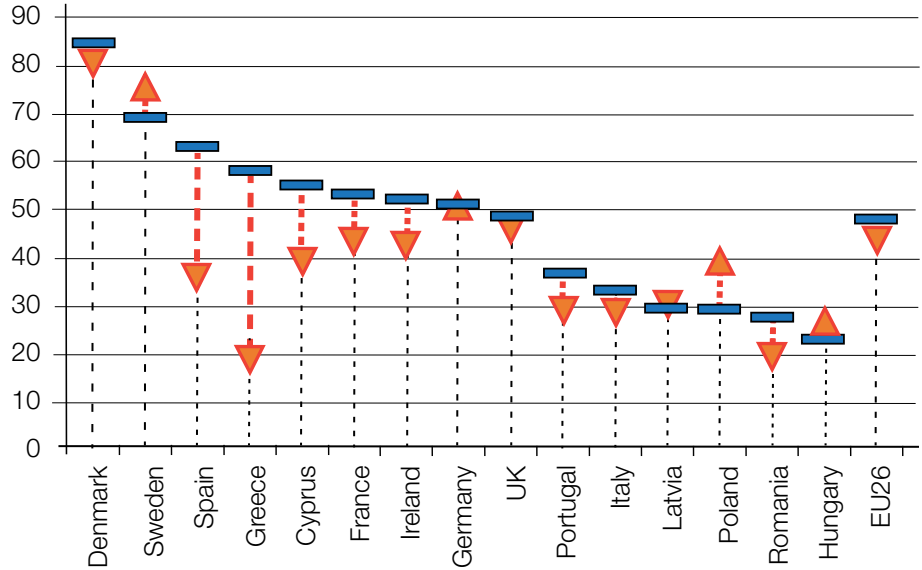
Professor Elsa Fornero's contribution to this volume focuses on her experiences

[14] Grafstein, R. (2015) Public pensions and the intergenerational politics of aging societies, *Journal of Theoretical Politics* 2015, Vol. 27(3) 457–484

in reforming the Italian pension system. She writes; "in principle, it would have been wiser to introduce reforms during a period of steady growth, when sacrifices would have been more easily acceptable than at times of recession… It lies however in the nature of electoral politics that political parties will be reluctant to "spoil" present good times by introducing painful reforms designed to prevent future problems". Ultimately in the case of Italy, it took imposition of a non-elected technical government in order to make reforms to the system. Democracy was, for at least a limited amount of time, put on hold.

But as events across the EU have shown, sudden and severe retrenchment at a time of economic turmoil comes with a heavy social and political price. Not only do such actions threaten incumbent governments, but they reduce trust in the institutions of government including support for democracy itself (see chart).

**Changes in support for national democracy (in % of population that tends to support) in selected EU countries 2007 – 2011**




Source: Democratic Audit[15]

[15] Armingeon, K, and Guthmann, K (2014) "Democratic Audit: The handling of the Eurozone crisis has undermined confidence in democracy across Europe" http://eprints.lse.ac.uk/57775/1/democraticaudit.com-The_handling_of_the_Eurozone_crisis_has_undermined_confidence_in_democracy_across_Europe.pdf. For the full academic paper see: Armingeon, K. and Guthmann, K. (2014) "Democracy in crisis? The declining support for national democracy in European countries, 2007–2011", European Journal of Political Research, Volume 53, Issue 3, pages 423–442, August 2014: http://onlinelibrary.

## Towards an unholy trinity

This contribution has argued that while democratic governments have been a key catalyst for expansion of the welfare state, the nature of electoral politics will make it difficult to reform key parts of the state. In particular, it has explored the potential for a great distortion of the welfare state, away from its role in supporting economic growth and social cohesion and increasingly skewed towards propping up age-related public expenditures. Such a distortion cannot continue indefinitely, as it will become unaffordable, and may require, at some point in time, enforced retrenchment which undermines the institutions and legitimacy of democratic government. The pace of such distortion will likely depend on the size and power of the older voting bloc, the ability of younger voters to mobilise, and the extent to which governments are concerned with balancing budgets over electoral cycles.

## Conclusion

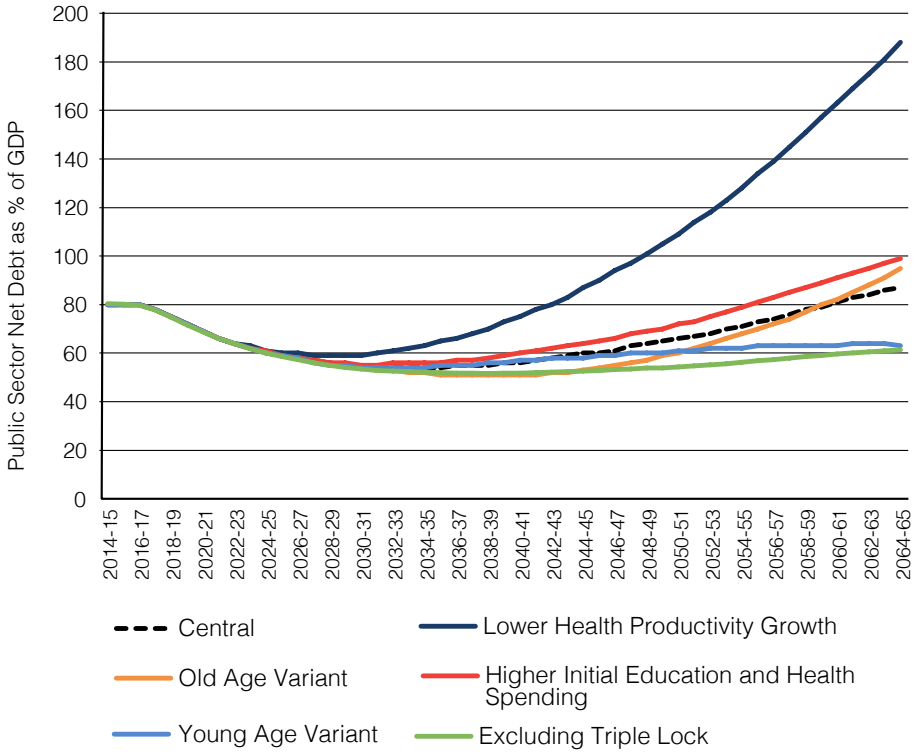
Reform does not just mean pulling back the welfare state. This essay has argued that the welfare state is both a means of providing people with essential services which the market does not provide, as well as being important in supporting economic growth which helps to sustain an ageing population. Reform is therefore likely to mean getting smart about which areas of state spending need to be expanded and which can be reduced. Such an effort should be based on an honest appraisal of how reforms will create winners and losers, and what measures are needed in order to manage and reduce adverse impacts.

In the context of EU-wide population ageing, the UK sits in an interesting position. It is not ageing as fast as many of our neighbours and has already undertaken reforms to the pension system to help support future affordability and coverage. As former UK Pensions Minister Steve Webb argues in his contribution, the mixture of automatic enrolment, move to a "Single Tier" state pension and raising the State Pension age, provides "the chance of a stable and sustainable regime for retirement saving". However, these reforms are just the beginning of an effort needed to renew and reorient the welfare state so that it is fit for the century ahead of us rather the one we have left behind. As the 2015 Office for Budget Responsibility projections show, depending on the policy choices we make and the pace of population ageing, debt as a proportion of GDP (a key measure of fiscal sustainability) could vary wildly over

wiley.com/doi/10.1111/1475-6765.12046/abstract

the long run (see chart). In this context, this volume of work seeks to outline what more needs to be done, not just to put us on a sustainable fiscal footing, but to ensure continual improvements are made to the health and wellbeing of our population.

**Debt to GDP projections: various OBR scenarios**




Source: OBR 2015 Fiscal Sustainability Report

# Distinctly average: The UK welfare state in context

Dr. Cesira Urzi Brancati, Research Fellow, ILC-UK

## Introduction

### About this contribution

This contribution explores the extent to which the British welfare state is better able to support the wellbeing of its citizens than other modern welfare states. It is only by understanding where the UK state sits today that we will be able to consider what types of reforms might be necessary in order to improve its effectiveness over the years ahead. This essay's findings are based on the ILC-UK's technical report published alongside this volume entitled "Measuring state effectiveness: the ILC-UK index".

### Background

The British welfare state was conceived as an antidote for the Five Giant Social Evils which had plagued British society before the war: ignorance, disease, idleness, squalor, and want.[16] In the landmark report 'Social Insurance and Allied Services', Sir William Beveridge argued that eradicating the five evils was in the interests of all citizens, and therefore, it was the duty of the state, as the representative body of all citizens, to bear responsibility for it. The report became a major propaganda weapon - it was dropped by parachute into occupied territory - and it was profoundly influential in the reconstruction of post-war Europe.[17]

The golden years of the British welfare state were relatively short lived. By the end of the 1960s, the post war economic consensus disintegrated and a new ideology, embodied by Margaret Thatcher, led to a series of reforms, which resulted in the state retreating from providing certain services, and changing the rules regarding entitlements to certain aspects of welfare support. While the Conservative government did not go as far in terms of privatization as it intended, the idea of relying on the market and self-responsibility was taken further in Britain than anywhere else in Europe.[18]

[16] Beveridge, W. (1942). Social Insurance And Allied Services; available at http://news.bbc.co.uk/1/shared/bsp/hi/pdfs/19_07_05_beveridge.pdf.
[17] Spicker, P. (2000). The welfare state, a general theory. London: Sage Publications
[18] George, V. and Taylor-Gooby, P (1996). European Welfare Policy; Squaring the Welfare Circle.

As the British case shows, the welfare state is a complex product of specific historical and cultural conditions as well as political compromises. Welfare states have evolved differently in different country contexts. Within Southern European countries, for instance, the welfare state has evolved around existing structures of familial support for elderly relatives.[19] By contrast, in Germany (and continental Europe), the Bismarckian scheme of social insurance, drew directly on the experience of workers' organisations in order to provide a model of stable finance and membership.

This essay will therefore seek to understand how well the UK welfare state model fares in comparison to its European counterparts.

## Has the UK succeeded at eradicating the Five Giant Evils?

We conducted a large scale investigation using data from the OECD and Eurostat to derive the State Effectiveness Index. The Index is a weighted measure of five other indices, broadly based on the Five Giant Evils: 1) poverty and social exclusion; 2) health of the population; 3) access to education; 4) quality housing; and 5) intergenerational fairness. The latter was not explicitly part of the Beveridge report, but has emerged as a major challenge facing modern welfare states.[20] In turn, each index is a weighted combination of several outcomes. We then rank 23 European countries against these indices (see Table 1).

### Overall results

At least one of the greatest social evils, squalor, is still endemic in Britain relative to other countries. With approximately 15 million people classified by Eurostat as at 'risk of poverty or social exclusion' (AROPE)[21] the UK is ranked 15th on the Poverty and Social Exclusion Index, followed only by Southern and Eastern European countries (as well as Ireland); similarly, it is ranked 14th on the Housing Quality Index, mainly because of its relatively high levels of housing cost overburden among the young and the working age population.[22]

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St.Martin's: New York.

[19] Tomassini, C., Glaser, K., Wolf, D. A., Broese van Groenou, M. I. and Grundy, E. (2004) 'Living Arrangements among Older People: An Overview of Trends in Europe and the USA', National Statistics, No. 115 (Spring). London: HMSO.

[20] To derive each of the five indices, we included a multitude of variables and performed principal component analysis. For a detailed description please refer to the technical report.

[21] At risk of poverty or social exclusion, abbreviated as AROPE, refers to the situation of people either at risk of poverty, or severely materially deprived or living in a household with a very low work intensity. (http://ec.europa.eu/eurostat/statistics-explained/index.php/Europe_2020_indicators_-_poverty_and_social_exclusion )

[22] Housing deprivation by age group is one of the variables used to derive the Housing Quality Index.

Against two other giant evils, disease (captured in reverse by the Health Index) and ignorance (captured in reverse by the Education Index), the UK performs relatively better when compared to the other EU nations but it is still mid-ranking.

The UK achieves its best results on the Intergenerational Fairness Index (IF), - 5th position. The IF index is a representation of how well younger and older people are doing compared to the working age group. A higher level of intergenerational fairness does not necessarily mean a higher standard of living for all generations, since if people of all ages are poor, they will also be more equal.

In terms of overall State Effectiveness, the UK is distinctly average – 11th out of 23. The Nordic countries, as well as Switzerland and several other Central European countries are ranked ahead of it, while much of Southern and Eastern Europe sits below it. Austria and Germany sit below us too, driven by relatively poor performance on health and access to education.

## Table 1: Country ranking by Outcomes (average 2003-2014)

| Country Ranking | State Effectiveness | Poverty and Social Exclusion | Health of the Population | Access to Education | Quality Housing | Inter-Generational Fairness |
|---|---|---|---|---|---|---|
| Switzerland | 1 | 3 | 1 | 11 | 11 | 6 |
| Sweden | 2 | 4 | 3 | 2 | 6 | 21 |
| Iceland | 3 | 1 | 2 | 14 | 10 | 3 |
| Norway | 4 | 2 | 7 | 3 | 4 | 20 |
| Finland | 5 | 5 | 15 | 1 | 1 | 9 |
| Netherlands | 6 | 7 | 8 | 10 | 12 | 1 |
| Denmark | 7 | 6 | 17 | 4 | 17 | 16 |
| France | 8 | 12 | 5 | 7 | 5 | 10 |
| Luxembourg | 9 | 11 | 12 | 13 | 3 | 19 |
| Belgium | 10 | 14 | 13 | 6 | 7 | 8 |
| United Kingdom | 11 | 15 | 9 | 9 | 14 | 5 |
| Ireland | 12 | 19 | 4 | 5 | 2 | 7 |
| Austria | 13 | 9 | 14 | 21 | 8 | 2 |
| Spain | 14 | 16 | 6 | 15 | 9 | 11 |
| Slovenia | 15 | 10 | 18 | 8 | 19 | 12 |
| Germany | 16 | 13 | 16 | 16 | 13 | 4 |
| Czech Republic | 17 | 8 | 19 | 20 | 18 | 13 |
| Italy | 18 | 20 | 11 | 22 | 20 | 17 |
| Greece | 19 | 21 | 10 | 17 | 21 | 22 |
| Slovakia | 20 | 17 | 22 | 19 | 16 | 14 |
| Portugal | 21 | 18 | 20 | 23 | 15 | 18 |
| Poland | 22 | 22 | 21 | 12 | 22 | 15 |
| Hungary | 23 | 23 | 23 | 18 | 23 | 23 |

Source: ILC-UK elaborations from Eurostat and OECD data (Pooled sample, 2003-2014)

## A closer look at the Indices: where do the evils find their strength?

*Poverty and Social Exclusion in the UK vs. the rest of Europe*

The Poverty and Social Exclusion Index is a weighted combination of the following measures:

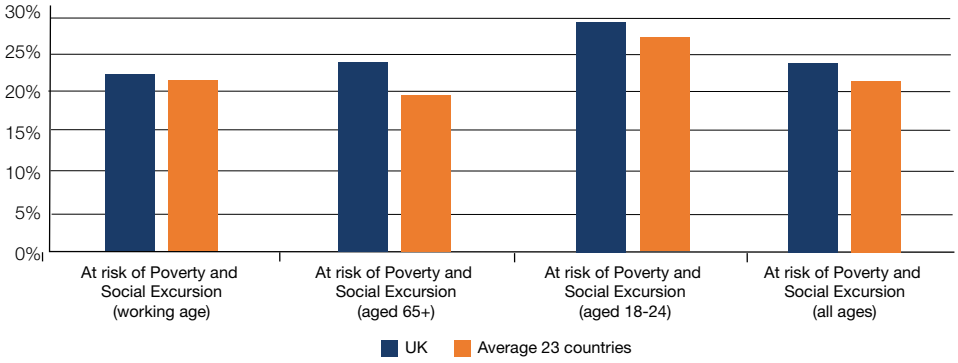
- Four indicators of poverty rates by age group;[23]
- Four indicators of risk of poverty and social exclusion (AROPE) by age group;[24]
- One indicator for the proportion of young people (18-29) Not in Education Employment or Training (NEET); and
- One indicator for pensioner well-being (replacement ratios) in all 24 countries between 2003 and 2013.

All measures are strongly correlated with each other, but there is huge variation across countries.

For example, risk of poverty and social exclusion for the total population ranges from 12.8% in Iceland to 34.1% in Poland; while risk of poverty and social exclusion in old age ranges from 7.1% in Luxembourg to 30.4% in Greece[25].

As Figure 1 shows, the UK fares worse than average in the 23 EU countries used for our analyses, but especially so in terms of old age people at risk of poverty and social exclusion.

**Figure 1: Proportion of Households at risk of poverty and social exclusion by age group (Pooled 2003-2014)**




*Source: ILC-UK elaborations from Eurostat data 2013*

[23] By poverty rates we refer to the proportion of households earning less than 60% of the median income.
[24] At risk of poverty or social exclusion, abbreviated as AROPE, refers to the situation of people either at risk of poverty, or severely materially deprived or living in a household with a very low work intensity.
[25] We are only considering the 23 EU countries which are part of our estimation sample and averaging risk of poverty and social exclusion rates between 2003 and 2014.

*Housing Quality in the UK vs. the rest of Europe*

The second indicator that reveals a particularly poor performance for the UK is the Housing Quality Index. The Housing Quality Index is a weighted combination of the following measures:

- Proportion of homeowners (with or without outstanding mortgage);
- Proportion of renters (market rent and social rent/reduced price rent);
- Housing overcrowding rate, by age group;
- Housing cost overburden / affordability;[26]
- Measures of housing deprivation: 1. dwelling too dark; 2. Lack of bath or shower; 3. Leaking roof / damp walls / floors / foundation or rot in window frames; 4. Lack of indoor toilet;
- Urbanisation level (proportion living in urban/rural areas);
- Composite index of severe housing deprivation by age category.

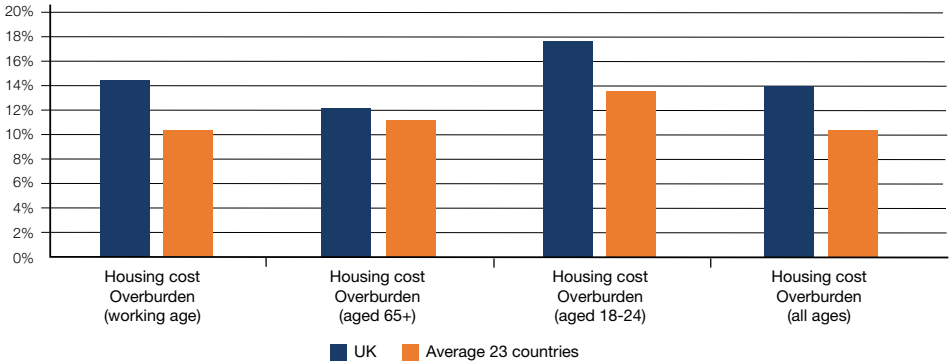
The UK is ranked 14th in the Housing Quality Index for a number of reasons: first of all, housing deprivation rates are higher than the EU average (17.7% vs. 15.8%); secondly, it has one of the highest rates of housing costs overburden, followed only by Germany, the Netherlands, Denmark and Greece[27].

If we look at the distribution of housing cost overburden by age, we see that the young (aged 18-24) are the most affected, both in the UK and in the EU, while the working age are the least. The lower rates of housing cost overburden among the old in the UK may, to some extent, offset, higher relative poverty rates among the old when calculated purely in terms of income. Indeed, once housing costs are taken into account, the poverty rate amongst the UK's working age population is higher than for the over 65s.

[26] The housing cost overburden rate is the percentage of the population living in households where the total housing costs ('net' of housing allowances) represent more than 40 % of disposable income ('net' of housing allowances).

[27] Even in this case, we calculated an average over 10 years for the 23 countries included in our final sample.

**Figure 2: Housing cost overburden (2004-2014)**




*Source: ILC-UK elaborations from Eurostat data 2004-2014.*

## Explaining mediocrity

### Approach and methods

While governments cannot directly control these outcomes, they have some indirect control through the welfare policies that they adopt. To help understand what drives the relative performance of countries on our league table, we first identified a large number of policies adopted by each state, and then explored how sets of interrelated policies aimed at achieving a set of goals relate to relative rankings on the league table.[28]

Examples of policy measures we selected are: spending on pensions or social protection as a % of GDP, spending on health, levels of contracting out to market forces, prevalence of means testing, classroom conditions, and many more according the availability of comparable data.[29] All individual policies were then combined through a statistical technique called principal component analysis to derive distinctive welfare strategies.

Our approach does not classify states as 'either/or', as in Esping-Andersen's welfare régime typologies, but identifies a state's underlying disposition; all states, to a certain extent, can adopt any welfare strategy, but some adopt a strategy more intensely than others, and this is what we capture in our analysis. A list of all 10 welfare strategies can be found in the technical report.

[28]Spicker, P. (2000). The welfare state, a general theory. London: Sage Publications
[29] For a complete list of all the variables included, please refer to the technical report.

## Findings

To help understand why the UK sits so low in the league table for Poverty and Social Exclusion and Housing Quality, we focused on welfare strategies that are successful at achieving higher rankings on both these outcomes. In this regard, there were only two strategies that were positively associated with better outcomes in both these areas:

- 'Welfare for families' (high expenditure on social protection, but especially on families, higher participation of older women in the labour force, and more universal welfare as in lower levels of means tested benefits).
- 'Innovative healthcare and sickness benefits' (i.e. substantial health expenditure, coupled with high tech hospitals, average number of beds, and high social protection on sickness).

Most of the countries typically defined by the first welfare strategy (Finland, Norway, Sweden and Austria) are also likely to adopt the second, with the exception of Luxembourg which scores really high on the first and fairly low on the second.

The UK has an intermediate score on both welfare strategies, which means that it is neither too strongly characterised by them, nor too weakly. By disaggregating the two winning strategies, we can see in which specific aspects the UK differs from countries with high scores.

With regard to the strategy 'welfare for families' we found that:

- Total expenditure on social protection in the UK is approximately 5 percentage points lower than in countries which typically adopt the 'welfare for families' strategy (approx. 21% of GDP vs. average of 26%);
- The UK's expenditure on social protection for families is about 1 percentage point lower than the average in countries that typically adopt the 'welfare for families' strategy (2.3% vs. average of 3.3%).

Similarly, with regard to the strategy 'Innovative healthcare and sickness benefits' we found that:

- The UK had a lower expenditure on healthcare as a proportion of GDP (approximately 1.5 percentage points less),
- The UK has a lower level of medical technology in hospitals or ambulatory, i.e. fewer healthcare resources, such as CT/MRI scanners, mammography units, per 100,000 inhabitants than most European countries (including

Turkey and most of Eastern Europe).[30]

- The UK has, on average, half the number of beds per 100,000 inhabitants compared to countries which score high on the 'Innovative healthcare and sickness benefits' strategy.

While the UK scores very poorly in terms of high tech medical resources, having a high tech system is not, by itself, a particularly strong predictor of good health or lower poverty rates (even though it does predict longer life expectancy). It is only in combination with the other measures included in the welfare strategy 'Innovative healthcare and sickness benefits' that it generates positive outcomes overall.

**Reform needed?**

The UK is the fifth richest country in the world with a GDP of £1.8 trillion.[31] And yet, one in four Britons, approximately 15 million people, can be classified as 'at risk of poverty and social exclusion' and the UK's performance on all six indices is mediocre relative to other European countries.[32]

Perhaps, given its relatively poor performance, the British welfare state is in need of reform. In this context, we have identified welfare strategies that are related to better outcomes. Our suggestion is that the UK might improve its position in the league table by adopting these strategies, or at least by incorporating some of the measures pursued by better performing countries.

Clearly it is hard to draw definitive conclusions on what works given the wide array of factors likely to influence performance over time. To complicate matters even further, incorporating different strategies may imply trade-offs so that improvements in some areas are offset by deterioration in others. However, the UK should and arguably could be higher ranked given its levels of prosperity, and adopting the right welfare strategies can influence its position.

Finally, it is perhaps worth mentioning the one welfare strategy, 'silver welfare' – typical of Italy, France and Austria – which is consistently associated with bad outcomes. With its high aggregate expenditure on social protection for old age (generally non means tested) and shorter working lives, silver welfare is the only strategy strongly predicted by the age structure of the population.

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[30] Source OECD Data, https://stats.oecd.org/Index.aspx?DataSetCode=SOCX_AGG

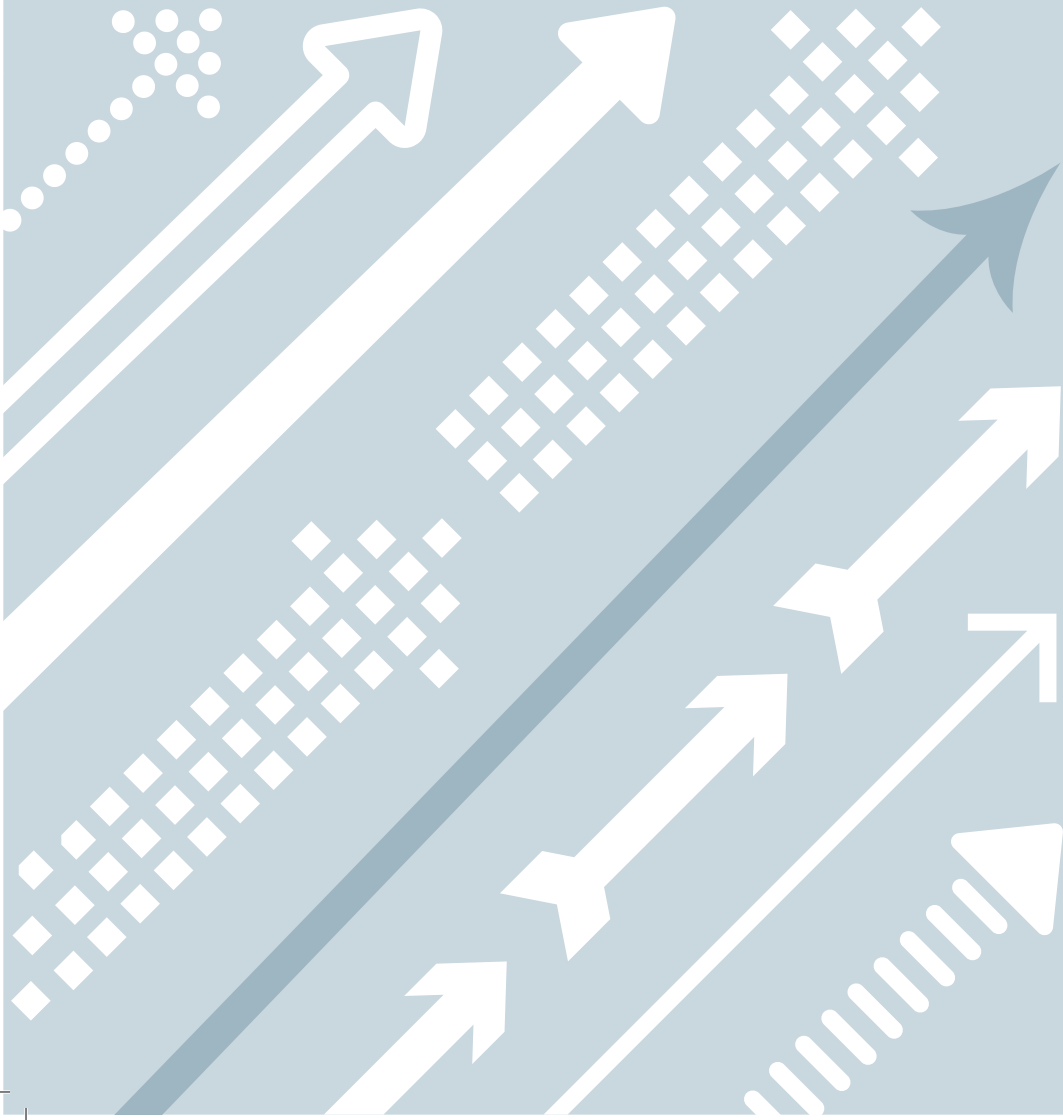
[31] IMF, World Economic Outlook Database (http://www.imf.org/external/pubs/ft/weo/2016/01/weodata/index.aspx).

[32] According to a more conservative indicator of risk of poverty, i.e. proportion of people with income below the 60% of national median, the number of individuals at risk is about 10 million.

The question is whether ageing societies, including the UK, will be drawn to silver welfare in the future, or whether we will be able to implement better strategies and avoid a likely increase in poverty and social exclusion.

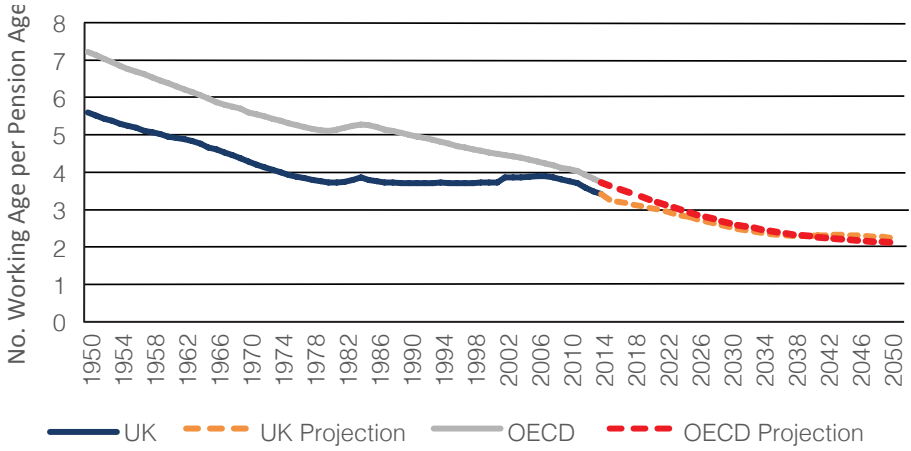
The UK must evaluate all its options carefully and choose the best welfare strategies, based on all the available evidence, to improve its rankings while minimising unintended consequences.

# **Part 2:** How population ageing is challenging the role of the state



# Population ageing

## Working age (20-64) per pension age (+65)

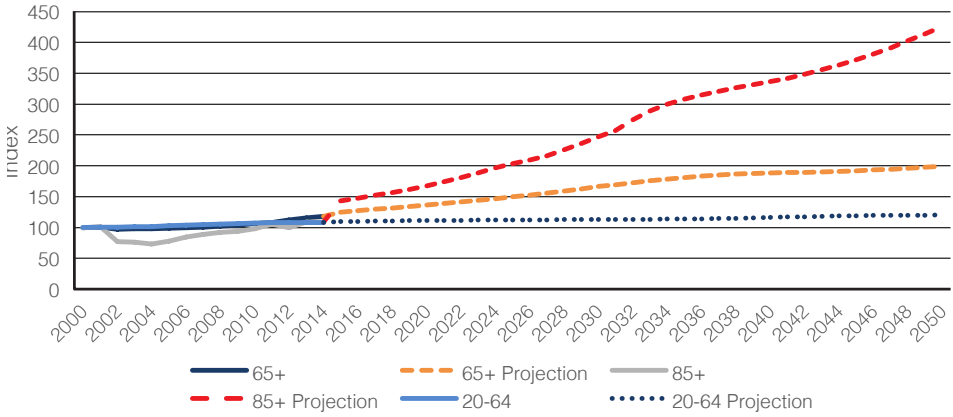



Source: OECD

**In 1950**, there were **5.5 working age people per person over 65 in the UK.**

**By 2014** this had fallen to **3.7** and it is **projected to fall to 2.2 by 2050.**

## UK population index by age (base year = 2000)




Source: OECD

**X2**

**By 2050,** it is projected that the **number of people over 65 will have doubled since the turn of the millennium.**

**X4**

**By 2050** it is projected that the **number of people over 85 will have increased fourfold.**

**+ 20%**

**However,** the population of **20-64 year olds** is only projected to **increase by approximately 20%** between **2000-2050.**

# Can we afford the welfare state?[33]

Nicholas Barr, Professor of Public Economics, London School of Economics [34]

## 1. Is a welfare state necessary?

There are powerful arguments for the welfare state: it addresses major market failures; by sharing risks, it facilitates economic growth; it pursues widely-supported equity objectives; and it contributes to social cohesion.

Important implications follow. First, to the extent that the welfare state has a significant efficiency role, opposition by libertarian writers is misplaced because it fails to take account of information problems, behavioural issues, and incomplete markets. Thus the right question is not whether to have a welfare state but what form it should take. That theoretical argument has historical support. Governments, including those of Ronald Reagan and Margaret Thatcher, came to power pledging to roll back the frontiers of the state. In practice, there was little change in welfare-state spending.

Once the welfare state's efficiency role is understood, this finding is not surprising. Social institutions are relevant to the population at large, not just to the poor. The welfare state is justified not only by redistributive aims but because it does things that private markets for technical reasons would either not do at all, or would do inefficiently. We need a welfare state of some sort for efficiency reasons, and would continue to do so even if all poverty problems had been solved.

That said, the welfare state is not a complete solution. It may make unemployment more bearable but does little to reduce the number of unemployed; nor does it improve working conditions; and many people, including women and ethnic minorities, are underprivileged for reasons not directly connected with poverty.

## 2. Is the welfare state desirable?

**Mistaken objectives?** Libertarians, espousing freedom and choice, argue that the welfare state threatens individual freedom. The validity of that view depends on the weight given to freedom compared with other objectives, and

[33] This chapter draws on Barr (2012, Ch. 13). Barr, Nicholas (2012), *The Economics of the Welfare State*, 5th edition, Oxford University Press.

[34] Professor of Public Economics, London School of Economics; N.Barr@lse.ac.uk; http://econ.lse.ac.uk/staff/nb.

also how freedom is defined: to a Libertarian, it means absence of coercion, to social democrats, freedom includes an element of security.

**An inherently mistaken enterprise?** Libertarians argue that a large purposeful collective enterprise is not possible, pointing to the coordination problems that beset central planning. However, the welfare state is not a monolith, but comprises smaller components. Secondly, many of these components are publicly *financed* but privately and competitively *produced*—welfare does not have to be state welfare. Thirdly, where market failures are severe, state action, albeit imperfect, may produce the least-bad outcomes.

**Damaging to economic growth?** Several arguments should be distinguished.

***Does the welfare state reduce growth?*** It is not controversial to argue that beyond a certain point higher taxation harms growth. What is controversial is (*a*) where that point is, and (*b*) the mechanism by which welfare-state spending might reduce growth. The issue remains disputed, as Atkinson (1995, Ch. 6)[35] makes clear.

- Welfare-state spending varies widely around the OECD average, with no evidence that growth has been slower in high-spending countries or vice versa.
- If the charge is that the level of welfare-state spending is too high, then, 'the Welfare State is no more than a co-defendant with other elements of the state budget' (p. 123).
- Causation can be problematic. Does higher spending reduce growth, or do countries with lower growth need to spend a larger fraction of GDP alleviating poverty?

***Are assessments of the welfare state well specified?*** The flaws in an argument that considers costs but ignores benefits are obvious.

'The emphasis by economists on the negative economic effects of the welfare state can be attributed to the theoretical framework adopted . . . which remains rooted in a model of perfectly competitive and perfectly clearingmarkets. *[This] theoretical framework incorporates none of the contingencies for which the welfare state exists ….* The whole purpose of welfare state provision is missing from the theoretical model'.[36]

[35] Atkinson, A. (1995), *Incomes and the Welfare State: Essays on Britain and Europe*, Cambridge University Press

[36] Atkinson, A. (1999), *The Economic Consequences of Rolling Back the Welfare State*, MIT Press.

Atkinson's point is that a model based on the assumptions of perfectly-functioning markets systematically rules out the market failures that it is one of the fundamental tasks of the welfare state to address.

***Is reduced growth necessarily a problem?*** Even if the welfare state reduces growth, that is not the end of the argument. If in state-of-the-world A ('capitalism'), there is rapid growth but little security, electorates may prefer to trade some growth for increased security, analogous to an insurance premium. At its broadest, this is a stylised representation of the development of the welfare state over the twentieth century. In state of-the-world B ('communism'), there is considerable material security but growth rates are low. People are therefore willing (as in the former Communist countries) to adopt market mechanisms, offering the potential for higher living standards at a cost of less security. In short, too little security reduces well-being; so does too much.

**Damaging incentive effects?** Some writers argue that social benefits, are not the cure to social ills but part of their cause, in that social assistance creates a 'culture of poverty'. The counter-view is that labour-market behaviour, crime, and single parenthood are far too complex to be explained only—or even mainly—by the incentives offered by social benefits.

### 3. Is the welfare state feasible?

**Even if the welfare state is desirable, does it remain feasible?**

**Is the welfare state compatible with a global economy?** Today much economic activity takes the form of computer-transmitted information. Thus national boundaries become porous, making competition global and reducing the freedom of any country to conduct an independent economic policy. The implications for the welfare state, however, are not necessarily apocalyptic.

***The world is not wholly global.*** Competition is powerful but not all powerful. Not all goods are tradeable. Nor are all factors mobile: labour mobility is reduced by choice (people prefer to stay with their language, culture and family) and because of constraints on migration.

***Western countries can adapt***. Box 1 summarises an important but often overlooked distinction between two ways – scale and structure – in which countries can adapt. Global pressures are not an argument for dismantling the welfare state, still less for radical structural change such as privatization. Rather, they are an argument for reducing the scale of some welfare-state activities.

***Newly industrialised countries may also adapt.*** Unless developing

countries are very different, rising incomes and the weakening of extended family ties will lead to demands for rising social spending in those countries. Thus a plausible outcome of global competition is some convergence.

**Box 1. What type of change: scale v. structure?**

It is important to keep two issues logically separate.

- What should be the *scale* of the state's activities—that is, the level of public spending on income transfers, health care, education, and the like?
- What is the appropriate *structure* of activity—that is, the public/private mix?

The first is largely a matter of budgetary balance—an issue of macroeconomics and political economy. The second is microeconomic. It is concerned with which activities are most efficiently privately financed and/or privately produced and which are not. The distinction is important: a budgetary crisis is *not* a reason for privatization.

**Demographically sustainable?** A range of policies address the problem of population ageing. Output can be increased by:

- Increasing the productivity of each individual worker, e.g. through higher investment in physical and human capital;
- Increasing the number of workers, e.g. by raising labour-force participation, raising retirement age, and/or by importing labour directly (immigration) or indirectly (exporting capital to countries with a young labour force).

If those policies are not a complete solution, demand can be reduced by reducing consumption by workers (e.g. through higher taxes or contributions) or by reducing consumption by pensioners (e.g. through lower monthly benefits). Thus the scale of pensions may need some reduction, but that is not an argument for radical change in structure.

**Compatible with social change?** Labour-market relationships and family structures have both become more diverse and more fluid. As a result, contributions related to employment are a less-good fit than in the past, suggesting that a non-contributory element in the pension system, as in

Australia, New Zealand, the Netherlands and Canada, is useful both to address elderly poverty and for reasons of gender balance.

**Compatible with economic crisis?** The economic crisis created pressures to reduce welfare-state spending (i.e. scale), but does not call the institution into question (structure). The argument that the crisis weakens the case for a welfare state is 180 degrees mistaken. Rather, the crisis emphasises the centrality of the welfare state as a device for risk sharing.

**A longer-term crisis of the welfare state?** Parts of the system certainly require change. And the welfare state is adapting.

- Demographic change means that pensions and health care will continue to face resource constraints, creating further upward pressure on retirement age.
- There will be mounting pressure for new insurance instruments (public, private, or mixed) to cover contingencies such as long-term care.
- New lending instruments will emerge. Income-contingent loans will increasingly pay for part of the costs of post-compulsory education and training.

**Politically sustainable?** The survival of the welfare state depends on political as well as economic sustainability. Libertarians argue that the state takes on tasks (e.g. the abolition of poverty) that are impossible, that failure undermines the state, and thus the welfare state contains the seeds of its own political demise. The exact opposite can be asserted. It is the welfare state that has made capitalism, with its attendant benefits of economic growth, politically feasible. Failure to address poverty can be destabilizing and politically damaging.

Discussion should not be about whether there should be a welfare state, but about its precise form and its distributional objectives. In reaching a similar conclusion, Glennerster points to two crucial sets of facts. First, the level of taxation and social spending varies widely and is not correlated in any obvious way with economic performance. Secondly, in the UK in 1945, 'in a ravaged economy, when real incomes were less than half what they are today, people voted for what came to be called the welfare state, and paid the price, and voted to continue affording it'[37]

[37] Glennerster, H. (1997), *Paying for Welfare: Towards 2000*, 3rd edn., Prentice Hall/Harvester Wheatsheaf

Thus the future of the welfare state depends not only on economic feasibility, but also very much on what people, through the political process, decide that they want.

## 4. Conclusion

A defence, however robust, understates the strong positive case for the welfare state.

- It exists not only to provide poverty relief (its 'Robin Hood' function) but also to offer insurance and consumption smoothing[38] (the 'Piggy Bank' function) in areas that private institutions are able to cover incompletely, if at all. It also has an important role in fostering social cohesion.
- There is increasing evidence that the roots of exclusion lie in early childhood, stressing the need for policies to support and enhance families. Such policies—a confluence of economics and social policy—involve cash benefits, health care, and education (including nursery education), alongside broader policies to improve parenting. Again, such activities require state action.
- The insurance element will become increasingly important. Risk and uncertainty are likely to intensify. An OECD report (2003)[39] emphasises natural disasters, technological accidents, infectious diseases, food safety, and terrorism. Actuarial insurance is not able to address problems of this type or on this scale. The 2008 economic crisis reinforces the salience of insurance.
- The previous point emphasises the importance of the welfare state as a device for risk sharing. Too little risk is suboptimal because it gives no incentive for risk-taking (e.g. low growth rates under communism). Too much risk is also suboptimal because it creates incentives against taking risks (in the absence of a safety net, a failed business start-up can leave a family destitute). Thus one of the purposes of the welfare state is to share risks optimally. From that perspective, far from being a regrettable necessity, the welfare state is an essential nurturing element in economic growth.

[38] I.e. redistribution from a person's younger self to his/her older self.

[39] OECD (2003), *Emerging Risks in the 21st Century: An Agenda for Action*, Paris: OECD.

# We need a new welfare model for the age of ageing

George Magnus, Independent Economist, Former Chief Economist at UBS Investment Bank and author of the Age of Ageing

As modern societies developed, welfare came to be an essential part of the social contract between governments and citizens. It has evolved mostly in piecemeal or incremental fashion, but every now and again, circumstances have demanded more comprehensive and institutional reforms that generate important political and social messages about economic direction, income distribution, dependency, and the nature and pattern of work. Now is such a time as we try to address the consequences of ageing populations in an environment, still constrained by the economic legacy of the financial crisis.

There have been several 'comprehensive moments' in the history of the welfare state. Bismarck's ground-breaking social insurance initiatives in the 1880s were triggered by the rising tide of German socialism. Britain had the Poor Laws earlier, but widespread poverty among a rising working class and the ascendancy of the Labour Party were instrumental in pushing the 1906 Liberal government towards a welfare system. The Great Depression spawned the US Social Security Act of 1935, and spurred William Beveridge's 1942 report, Social Insurance and Allied Services, which was the foundation for the creation of the modern UK welfare state.

A new comprehensive welfare reform programme is needed today for two reasons. First, the unique human experience of rapid societal ageing has rendered our inherited welfare model unaffordable and obsolete. We have to develop coping mechanisms to mitigate the economic and financial effects of population ageing. Second, although welfare reforms have figured prominently in the wake of the 2008-09 financial crisis, they have been driven by the perceived need for immediate reductions in public spending, not the need to re-design welfare for an ageing society. Some changes, such as raising the pensionable age, do serve both purposes, but important ageing issues have not been properly discussed.

One of the most important, perhaps, is the vexed one of who should pay for our ageing population, and how the generational burden should be distributed.

There is a strong case, therefore, for a broader public debate about the welfare entitlement rights and obligations of the government and citizens in a demographic environment that is unprecedented.

**A unique human experience needs new thinking**

As individuals, we are happy to celebrate rising life expectancy. Last year, the UK had over 3 million people aged over 80, and 16,000 centenarians. By 2040, it is predicted they will have grown to 5.5 million, and 52,000, respectively, and they will keep growing rapidly thereafter.

Collectively, though, we have an economic problem. As a result of the unprecedented combination of weak or falling fertility, and greater longevity, the working-age population (WAP) is going to stagnate or fall. In the UK, it will grow very slowly, but in many other countries, including Germany, Italy, Russia and China, which is the fastest ageing country on Earth, the WAP is falling and will continue to do so for the foreseeable future. In the UK, the population of people aged over 65 as a proportion of the WAP, known as the old age dependency ratio, is predicted to rise from 26 to 40 per cent by 2040. Put another way, the number of working age people supporting each person over 65, will drop from 4 to 2.5.

At a macroeconomic level, we should expect - and are already seeing to a degree - lower economic growth, savings, investment and productivity growth, and a relentless rise in age-related spending, that is, pensions, healthcare and residential and long-term care. Other phenomena that have become more obvious or urgent include the inadequacy of retirement savings; the need to try and increase labour force participation further for older workers; unsuitable work and retirement patterns; and rising stress in the social and health care systems.

The funding crisis in the NHS, for example, has been widely publicised, and is only likely to deteriorate as things stand. Indeed, according to the King's Fund, a health research charity, NHS spending, despite being ring-fenced from cuts, will fall from 8.5 per cent to 7 per cent of GDP by 2020 in the face of unstoppable and increasing demand. But the NHS needs to invest more not only in doctors and nurses, and hospitals and equipment; it also needs to invest in the changing epidemiological and health needs of an ageing population. A recent OECD report, for example, has highlighted the need to exploit 'big data' to bring together massive and complex records of administration, and clinical,

biological, and palliative care[40].

## Age-related spending

Estimating the future costs of age-related spending by governments is fraught with difficulty. Laws may change, we can only guess what future economic growth will be, and we don't know how effective our coping mechanisms will be. These include possible further increases in the pensionable age, changes in work and retirement patterns to permit older workers to stay at work into their late 60s or 70s, higher levels of immigration if politically acceptable, and ultimately, policies designed to raise productivity.

As things stand and on the basis of current laws, though, the additional age-related spending needed in the UK by 2040, for example, is thought to be about 2% of GDP, rising to 2.4% by 2060, according to a recent study by the European Commission[41]. This doesn't sound a lot, but it is a measure related to GDP in the future, which is expected to be appreciably larger than today. It means that age-related spending has to grow consistently faster than GDP, and that we will not be spared periods when borrowing or taxes have to rise, and or other public spending will be subject to restraint.

Think of it another way. If the government had to write a cheque today to cover the costs of known increases in pensions and healthcare in the future, it would amount to about 60 percent of 2013 GDP. This 'net present value' estimate of the anticipated rise in age-related spending was made in a report to the European Parliament in 2014[42]. The UK costs were not the highest, and were exceeded by a significant margin by the US, Belgium, the Netherlands, South Korea, Switzerland, Austria and Finland. Austerity policies and welfare reforms in recent years, especially in the EU, have lowered these future costs in several countries, but they remain considerable.

## Who will pay?

These policy changes have proven contentious, prompting additional concerns about income inequality and inter-generational fairness. They are sure to persist in the face of the relentless increase in the age structure of our societies. Hence, the need to consider perhaps radical changes in the ways in which we organise, fund, provide and deliver welfare, and age-related spending in particular. The

[40] OECD "Data-Driven Innovation: Big Data for Growth and Well-Being" October 06 (2015)
[41] The European Commission "The 2015 Ageing Report: Economic and budgetary projections for the 28 EU Member States (2013-2060)" European Economy (2015)
[42] Mauro, P. (2015), "Debt sustainability and economic convergence of euro-area Member States: Challenges and Solutions" Peterson Institute of International Economics, European Parliament

economy and our demographics today, after all, bear little resemblance to what they were in the 2000s, let alone to the early decades of the post-war period when our welfare systems were built and expanded. In short, we have spent our so-called demographic dividend - or the economic benefits we get from rising numbers of people at work before old age dependency rises - and the welfare model needs to be refreshed, but how?

There is no single or simple answer. Age-related spending is in continuous competition with other forms of spending that also have strong claims on resources, especially when we are also trying to lower the share of debt in relation to GDP. Moreover, coping mechanisms will take time to develop. We should start, however, by asking serious questions about the extent to which we think older citizens, themselves, should contribute.

In the UK, we have come a long way since Peter Townsend's 1979 report, "Poverty in the UK', in which he highlighted 40 per cent pensioner poverty rates and 'old people' being systematically ignored by politicians and the public[43]. The poverty rate in 2013/14 was 14 per cent, compared with more than double that rate in 1998/99. It is below that of working age people without children, and far below those with them. The recently retired and those close to the state pension age, in other words, are mostly much better off absolutely and relative to their antecedents.

**Pensions, other benefits and housing**

According to the Office of National Statistics (ONS), the mid-point pensioner income is about the same as for working age people. More than 40 per cent of pensioners are now in the top half of the income distribution. Further, the median disposable income of retired households was over 7 per cent higher in 2013/14 than in 2007/08, while that for non-retired households was 5.5 per cent lower[44].The Institute for Fiscal Studies has demonstrated that pensioner incomes remained stable at about 60-70 per cent of non-pensioner incomes from the 1960s to the 1990s, but then soared to 90 per cent by 2013/14, or 102 per cent after taking into account housing costs[45].

UK pensioners have enjoyed an additional benefit put on the table not as a result of primary legislation but by a government manifesto commitment. This is the so-called 'triple lock', a formula according to which the State Pension rises

[43] Townsend, P. (1979) "Poverty in the UK: A survey of household resources and standards of living" Harmondsworth, Penguin Books.
[44] Results from the OECD exercise on the distribution of household income, consumption and savings
[45] Belfield, C. Cribb, J. Hood, A. and Joyce, R. (2014) "Living Standards, Poverty and Inequality in the UK: 2014" The Institute for Fiscal Studies.

each year by the greater of average earnings, the consumer price index or 2.5 per cent. According to a report from the Government Actuary's Department, taken off-line almost as soon as it was published, the triple lock will add about £6 billion to the pension bill in 2015/16, and would, if retained after 2020, add about 9% to National Insurance benefit payments by 2040, rising to 23 per cent by 2070, compared with a simple earnings uprating.

Retired households, of course, still show wide diversity in terms of income and wealth, as evidenced by the 2.4 million pensioners that claim pension credit. Yet, income inequality in the retired household sector is bigger than it is in non-retired households. The richest 20 per cent received 56 per cent of basic (pension and annuity) income, compared with 46 per cent for the top quintile of non-retired households. Private pensions, especially from now almost defunct final salary schemes, have grown significantly in recent years to account for 42% of total income, which also includes various cash benefits provided by the government.

These cash benefits comprise assistance to those in need, and also to those who have no need and take the form, for example, of winter fuel payments, free TV licenses for the over 75s, free bus and other transport passes, and prescription charge exemptions. The NHS is, of course, free to all. In addition, those who reach State Pension Age and continue to work benefit from not having to pay National Insurance, while tax-free pension lump-sum payments are also permitted.

Today's retired households have also enjoyed a significant wealth effect from housing. The ONS points out a major generational change in the profile of home ownership, in which the 65-74 year olds cohort is the group most likely to own their home (8 in 10), while about 60 per cent of over-65 home owners have no mortgage debt. It points out, not coincidentally, that in the early 1990s, home ownership was much more concentrated among 35-44 year olds. The baby boomers, in other words, have not only fared better than their parents, but have set standards their progeny may never realise, certainly as far as property ownership and affordability are concerned[46].

**What to do?**

It will take time to develop the coping mechanisms needed in ageing societies, but if successful, these should raise the economy's potential growth rate, and mitigate the economic consequences of ageing arising from labour force

[46] ONS, Housing and Home Ownership, January 2015

constraints. We may even find that if labour becomes sufficiently scarce - and it is starting to show in occupations with greater skill and educational attainment levels - wage and salary formation will strengthen for working-age people. This would certainly qualify as an additional coping mechanism for those retiring in coming years.

In the meantime, and while many of these mechanisms evolve, we should also debate how we think ageing societies should be financed and funded. The case presented here is that from an equity and inter-generational fairness point of view, we should be prepared to consider, borrowing from Marx, from each according to their income ability to each according to their need. Certain policies would then merit immediate consideration. These include bringing the triple lock pension arrangement to a close, and placing limits on winter fuel, transport passes and TV licenses.

After this, the politics become more contentious. Yet, age and healthcare research professionals have argued that National Insurance could be levied on retired individuals at a reduced rate, and tax relief on pension lump-sums and contributions could be reconsidered or redistributed. For example, tax relief on pension contributions, tax-free growth in pension assets, and a 25% tax-free lump-sum on retirement don't have to be an entitlement for all, regardless of income and size of pension pot. Considerable revenues could be raised by a modest additional National Insurance levy on 40-65 year olds and on top income earners. Think of this as a sort of pay-down on future age-related spending from which they would benefit, while not burdening the youngest workers with something to which they would understandably find it hard to relate. We might also have to put other taboo topics on the table for review, such as the mix of public and private healthcare funding, prescription charges and exemptions, and even possible selective charges for some types of treatments and procedures.

This will be an awkward and politically sensitive discussion. It will challenge hitherto sacrosanct ideas such as universal benefits, and a sort of inverted means-testing for better-off citizens. It will raise the charge that older, and theoretically more vulnerable, citizens are being targeted. It will require the government, employers, and labour organisations to subordinate political and vested interests to the task of reforming the model of financing and delivering welfare. Hard as that sounds, the simple truth is that the current entitlement structure is unsustainable. It would be better to amend it under modest than extreme duress.

# What the welfare state is for

David Willetts, Executive Chair of the Resolution Foundation and Visiting Professor at King's College London

The idea of the welfare state was formulated to mean a state committed to the welfare of its citizens. Beveridge and his generation were clear that this meant social security delivered through social insurance. It did not require the full panoply of national insurance contributions, though that was preferable. The core idea was mutual insurance – we were all at risk from adverse life events which were either unavoidable, such as ageing, or at least risks to which we were all exposed, such as unemployment. This mutual insurance had to be supplemented by something rather different, less legitimate and less desirable, means-tested social assistance. It was less legitimate as it did not rest on the same principle of mutuality: instead it was redistributive from prosperous to poor, from "us" to "them".

The gap between these two different forms of state action is very clear in the US where there is a distinction between popular programmes such as social security or Medicare and something very different whose political support is far lower – welfare. When Americans worry about welfare dependency they are not talking about social security for pensioners: they mean programmes such as food stamps or help for lone parents.

We had a similar distinction here. Margaret Thatcher's first ministerial post was Parliamentary Under Secretary for National Insurance and when I worked for her she would ask me detailed questions about the contribution requirements for specific benefits. Her thinking on the subject had been shaped by Beveridge. He had tried to roll back means-tested assistance by designing a system of mutual insurance which would cover unemployment, ill health, and retirement.

Now there is a creeping linguistic advance of "welfare" which is sometimes used to describe all transfer payments. The State Pension becomes welfare and so does Child Benefit. This is not how the word "welfare" was historically used in Britain: it is an imported Americanism but extending its meaning very significantly in the process. This matters because it leads to the assumption that the role of the welfare state is to redistribute from rich to poor. This is certainly a duty that the State must discharge in certain circumstances, and the incidence and extent of these will be contested endlessly by the Left and Right.

But such a description misses out the crucial Beveridge-inspired role of the welfare state – which has historically garnered support across political dividing lines – in providing mutual insurance.

This trend is reinforced by a second crucial confusion of terms which is to treat targeting as synonymous with means-testing. Means-testing is one way in which public programmes focus on poor people. It was the basis of national assistance, which became supplementary benefit which became income support which became part of tax credits – the repeated changes of name reveal the lack of legitimacy of the programme. But one of Beveridge's great insights was that if you define the category of entitlement to benefits carefully they can be quite well targeted without the need for means-testing. So being retired or being unemployed or being sick were likely to be associated with a low income so programmes aimed at these categories of people were well-targeted without being means-tested.

These changes in the way we think about the welfare state have eroded our understanding of its mutuality – our understanding of it as a shared insurance pool to which we all contribute through our taxes and contributions and which we can all draw from when we are old or face the additional costs of children.

This mutuality comes in different forms but the most important form is between the generations. This underpins not just the welfare state but it is the contract which underpins society as a whole. We can see that by going back to a primitive society without money or government and measure not money but calorie consumption. Anthropologists have studied these patterns in tribes in the Amazonian Rain Forest or the jungles of Central Africa. They find of course that when we are children we are net consumers of calories as our ability to produce them ourselves by hunting or fishing are limited. In adolescence we do start contributing calories to the tribe but we are still learning which berries we can pick – as we go after high value difficult food it takes a lot of education to get. Then in adulthood we become net contributors of calories to the tribe. Perhaps as you read this a forty-year-old is staggering back to the tribal embankment with four fish after a hard day's hunting, thinking to himself that he will be lucky to get one after they have been eaten by the children and the rest of his clan. As we get older our capacity to hunt or pick berries declines and we become once more net consumers of calories. The key ages of transition to net production occurs about 16-18 and back to net consumption in the late 50s. This is a kind of welfare state and it provides a clue to how it works. It works by exchange between the generations.

At any one moment it looks like one generation giving to another but that is not the whole story. We do that so we can smooth our own income and consumption. When the elderly tribesman dies his calorie consumption and production should net out and be in balance. Paul Samuelson summarised it very well in a classic paper: "giving goods to an older person is figuratively giving goods to yourself when old." The exchange between the generations is how we smooth our own income across the life cycle. This reveals what the welfare state does but also how it can go wrong. It depends on the mutual obligations between generations but that can go wrong if individual generations fail to keep their side of the bargain, deliberately or accidentally, break their part in the contract. That can mean expecting to be generously funded during the periods when they are net recipients from other generations but not paying their share during their years of maximum production. But these breaches in the contract between the generations need not occur because of malevolence – they can also be the result of lack of understanding or changes in circumstances.

So for example imagine you have a rule that the budget should be balanced across the economic cycle and you maintain stable real spending on each child's education and each pensioner's benefits. Then there is a surge in the birth rate so that there are more children. This pushes up public spending and taxes have to go up. When this big generation reach working age they have fewer elderly dependents ahead of them and fewer young people coming after them so there is less public spending pressure and their taxes can be cut. But when they become pensioners these pressures increase and taxes on the working generation behind them have to rise. This is a schematic example of how a big generation can gain disproportionately from the welfare state. But in fact it very closely resembles the UK experience, driven by the baby boom between 1945 and 1965, when births per year rose from the long-term average of around 750,000 to in excess of 1 million in the peak years.

Another example of how this can happen is if pension entitlements are set at a fixed chronological age but there are substantial and unanticipated improvements in life expectancy. That makes those claims on resources much more valuable or onerous, depending on one's perspective. Eventually public policy catches up and we index pension age to life expectancy but meanwhile a lucky generation has enjoyed an uncovenanted benefit. Again, this is a good description of recent UK trends. Health improvements have accelerated life expectancies, and the generation of boomers currently reaching retirement are cashing in during the State Pension Age catch-up period.

There have been ingenious attempts to monitor the effect of tax and spending policies on specific cohorts to see if there are some who do well out of the welfare state compared with others. John Hills carried out such an analysis and identified that the cohorts born at the beginning of the twentieth century did well from the creation of the welfare state. Then there was a dip. The baby boomers, born between 1945 and 1965 do well and are net beneficiaries but then there is another decline so that younger generations end up as substantial net contributors. These estimates depend on heroic assumptions about future policy so that they can cover the full life cycle of today's cohorts. We hope at Resolution Foundation to conduct an important exercise to update these estimates.

Meanwhile we can track specific changes in the value of benefits for different generations. There are substantial reductions in the value of benefits for working age adults. This is a striking contrast with the triple lock for pensioner benefits which means they increase by prices or earnings or 2.5% whichever is highest. As a result, our projection is that by the end of this Parliament welfare payments per-working age adult are set to be 9% lower in real terms than pre-crisis, while pensioner payment will be 13% higher.

This very generous protection for pensioner benefits has brought us to the situation where pensioners are now less likely to be managing on low incomes than then rest of the population. It is good news that we have had such success in tackling pensioner poverty. But it does mean that now the challenge is to tackle low incomes affecting different generations and other stages of the life cycle. In finding the resource to tackle this we might reflect on the cost of maintaining a range of schemes helping older people from winter fuel payments, free TV licenses and free public transport in London for all the over-60s. One quarter of the journeys taken by these over-60 passengers are to work – evidence of how these special perks have failed to keep up with the changes in the distribution of income and the pattern of the labour market.

The good news however is that people are increasingly aware of the importance of inter-generational fairness. These elderly people are not greedy geezers who pursue their own self-interest at the expense of other generations. One reason they care about inheritance tax is that they see the equity in their house as savings they wish to leave to their children and grandchildren. The increasing publicity given to warnings about the housing crisis facing younger people also appears to be leading to a shift in attitudes with Social Attitudes Surveys showing the proportion of the population supporting more house-building

has doubled from 27% to 54% between 2010 and 2014. Meanwhile young people themselves clearly feel a sense of obligation to the older generation – they register quite high levels of support for pensioner benefits, perhaps because they think this is what their granny needs. So the contract between the generations has not been destroyed: it is still present in popular attitudes. The challenge is to ensure that our policies are kept up to date so that the welfare state properly discharges it rather than distorting the balance between the generations

# Towards economic stagnation? How falling fertility is leading to sterile economies

Norma Cohen, Former Demography Correspondent at the Financial Times and currently a PhD candidate at Queen Mary University of London (QMUL)

'Make Room, Make Room!', Harry Harrison's dark novel of 1966 depicted a vastly over-populated world in which humans, particularly the elderly, are forced to scrounge for the scraps of sustenance they can find. Set in a future 1999, global population had swelled to a dangerous 7bn people, more than anyone could imagine then.

Fast forward to 2016, global population is 7.3bn and set to rise to 9.7bn by 2050 according to projections from the United Nations Population Division. And far from starving, the elderly in industrialised nations are protected by social insurance schemes that, as in Britain, some are arguing are too generous. But Mr Harrison's book contains a kernel of truth; population does matter, although it is becoming apparent that its 'shape' matters perhaps even more than its absolute size. While overall population is growing, much of that comes from the rising numbers of older people. With the exception of parts of sub-Saharan Africa and the Middle East, fertility is – and has been for decades – falling, so that new entrants to the workforce are growing much more slowly, and in some countries, are actually declining. And while much of the focus on population change has been expressed as concern about the affordability of state old-age pensions and health care systems, there is perhaps a larger worry; that is, does population change produce a drop in demand that cannot be offset through lower interest rates, therefore implying a stagnant economic future.

In a recent issue of Foreign Affairs, Ruchir Sharma, head of Emerging Markets and Global Macro at investment bank Morgan Stanley, notes that this slowdown in growth among the working age population globally is one of the key reasons why economic activity has failed to rebound from the 2008 financial crisis. Much of the global population growth in recent decades has been amongst those aged 50 and over, and in particular, the over 80s. "(This type) of demographic decline is toxic for the economy," he notes. "The primary threat most countries

now face, in fact, is not too many people but too few young workers.[47]"

If there really were too few young workers to meet the demand for output in countries with ageing populations, you would expect to see wages soar as employers compete for scarce labour. But that is not what is happening; instead, demand remains sluggish and wage growth is weak. And while there are several plausible explanations about why this recovery has been so weak – high levels of indebtedness, growing income inequality to name but two – the sharp slowdown of working age populations is undeniable. Between 1960 and 2005, the global labour force grew at an average annual rate of 1.8 per cent. But since 2005, that has slowed to an average of 1.1 per cent per year.

Mr Sharma is hardly the first economist to point to demographic change as a driver behind slowing economic activity and low inflation. Indeed, in the debate about whether the industrialised world has entered a period of far slower economic growth than that which characterised the post-war years despite interest rates at close to zero, one of explanations is that of demographic change. Economists such as Harvard's Larry Summers and Robert Gordon of Northwestern University, have raised the possibility that the industrialised world has entered a phase of 'secular stagnation', of which one driver is the rising percentage of older adults in the population. Economists broadly define secular stagnation as a world in which demand for capital equals the pool of savings only when real interest rates are negative. In a paper for Vox.EU, economists Juan F. Jimeno, Frank Smets and Jonathan Yiangou point out that Europe's demographics may result in an even bigger savings glut in the future than exists today[48]. As it becomes increasingly apparent that current public pension systems cannot sustain current levels of benefits, private savings are likely to increase. "Some of the long-run trends appear largely irreversible," the economists note. "Demographic patterns in particular are characterised by significant inertia. Even with some recovery in the fertility rate, increases in retirement age, and higher immigration flows from outside Europe, the ratio of the retired population to the working age population will continue rising strongly."

The reason demographic change is so crucial to economic growth is three-fold. First as older adults enter retirement, generally defined as the age at which

[47] Sharma, R. (2016) "The Demographics of Stagnation: Why people matter for Economic Growth" Foreign Affairs, March/April

[48] Jimeno, J. Smets, F. and Yiangou, J. (2014) "Secular Stagnation: A view from the Eurozone" featured in Secular Stagnation: Facts, Causes and Cures, Centre for Economic Policy Research

they can receive state pensions, they drop out of the workforce. An ageing population may therefore imply a shrinking or stagnating workforce. Second, the so called "retirement consumption puzzle" means that individuals reduce their consumption in retirement. An ageing population may therefore act as a drag on aggregate demand as consumption expenditure falls. Third, older adults are likely to favour safe assets such as government bonds rather than equities. An ageing population may therefore imply a shift in asset allocation away from risky assets which help support investment in the economy and drive up real interest rates and towards safe assets.

## A stagnating/shrinking working age population

As retirees, they are no longer contributing to the output side of the GDP equation. This may be part of the reason why economic activity has been so slow to recover after 2008; the post-war baby boom that produced such a spectacular bulge in the workforce in previous decades is now old enough to retire. Economists point to workforce participation rates in the US, which historically has had high rates relative to those in Europe. The US post-crash workforce participation rates reached a trough of 62.4% in September 2015 but as of February 2016, was beginning to climb again, according to economists at Barclays Bank. But the 66 per cent workforce participation rate as at December 2007 would have begun to fall anyway, the economists note. "In other words, demographics alone have shaved two percentage points off participation, as the large baby boomer generation started to reach retirement age around the start of the recession." The UK had a somewhat different post-war baby boom, but it, too, is reaching the age at which withdrawal from the workforce is not only possible but generally expected.

## Older people are failing to consume

Compounding the effects of a dwindling workforce is the fact that, as age increases, consumption spending recedes. Thus, an economy with a growing proportion of older adults faces a drop in demand growth. Anyone wanting to see how this translates into consumption need look no further than the Office for National Statistics' Living Costs and Food Survey which categorises expenditure by the age of the 'household reference person'. Analysis of the data by the International Longevity Centre-UK found that as people get older, they spend progressively less on consumption, regardless of their income. A household headed by someone aged 80 and over spends, on average, 43% less than a household headed by a 50-year-old. And this pattern of declining

consumption is common to different income groups. A low earning household consumes, on average, about 113.7% of their income at age 50 and about 75.7% at age 80 while higher earning household consumes only 67.7% of their income at age 50 and about 62.6% at age 80[49].

Nor is Britain an outlier when it comes to consumption patterns of older adults. Data from the US Census Bureau's 2014 Consumer Expenditure Survey shows a similar pattern. Households headed by a person aged 65 or older are 23% of all households, but account for only 18.1% of total food expenditure and 13.8% of apparel and services spending. Again, spending for those aged 75 and over, is even more subdued; these account for just under 10% of all households but 6.2% of food spending and 3.7% of apparel spending. There are categories of outlays for which older households are disproportionate spenders. These include rental accommodation and household personal services. Importantly, these data do not include the effects of intergenerational transfers in the form of social and health care spending. Taking these into account would produce a vastly different picture of consumption among older adults.

## Savings may be "safe" but not "productive"

To some extent, the weak consumption among older adults is partly offset by intergenerational transfers of individual wealth. When individual wealth is saved, it represents deferred consumption, a process described as 'consumption-smoothing'. If not consumed, it is passed to children and grandchildren and consumed with gusto in later years. However, intergenerational sharing also occurs through fiscal measures where working populations today are taxed to pay for the elderly and children.

Social security systems consume income of today's workers to pay for today's retirees. When today's workers are taxed to pay for tomorrow's workforce – today's children – it represents an investment in human capital that will deliver higher productivity tomorrow. There is also a third channel through which a rising proportion of older adults will influence economic activity. That is, as they age, households store capital and increasingly look to invest in 'safe assets', those delivering a secure, if lower, return. This savings habit may be one of the reasons why real interest rates have remained so low.

[49] Brancati, C. Beach, B. Franklin, B and Jones, M. (2015) "Understanding Retirement Journeys: Expectations vs Reality", The International Longevity Centre-UK

## Ageing as an international phenomenon

Ageing populations are a characteristic not only of mature, industrialised economies, but also of some newly emerging economies particularly in East Asia. The reasons for the population shift have been twofold; first there has been the remarkable rise in longevity. Although life expectancy at birth has been rising in the developed world since the 19th century, that was mostly achieved through reductions in infant and child mortality. But particularly since the mid-20th century, life expectancy at older ages has been rising rapidly and not just among wealthy nations but also among some of the world's poorest. According to data from the United Nations' Population Division, life expectancy at birth in the developed world was 65 in 1950. By 2010-15, it was estimated at 78 years and is rising further.

But improved longevity is not the sole explanation for the rising percentage of older adults globally. Perhaps even more important has been the collapse in fertility rates. Demographers calculate that each woman must produce 2.1 children, on average, over her lifetime to keep a population broadly stable. Today, UN data show, roughly half the world lives in nations where fertility rates are below 2.0 per woman. Europe has been characterised by flagging fertility since at least the 1980's – children born in that year would now be prime working age adults of 46 years – and the trend accelerated through the 1990's and early 21st century. Not one European country is producing enough babies to keep their populations stable, although France is close.

Thus, global greying does not simply represent the triumph of medical science over many deadly diseases. It represents a collapse in the rate of production of new human beings across the globe generally and in East Asia and Europe in particular. Britain, for the most part, has actually experienced a population shift that is less dramatic than that of many of its European counterparts, partly because of its status as a magnet for migrants. Currently, the percentage of the population aged 65 and over is 17.7%, the highest ever, and up from 15% in 1981, despite a surge of working-age migrants since 2004. The EU data also show that Britain has done somewhat better than average on the fertility front; in 2014, the rate was 1.81 births per woman compared with an EU-28 average of 1.58 births.

For countries contemplating measures to offset the economic effects of ageing – and not simply the fiscal effects of increasingly unaffordable old-age insurance – Japan is an instructive lesson. It has been the poster child

for an economy struggling with the economic effects of not only an ageing population, but a dwindling one as well. Overall, its working age population has been declining since 1995 and the absolute size of its population since 2007. But between 1955 and 1975, its overall population and working age population rose by 1.3 and 1.8% annually. Masaaki Shirakawa, a Governor of the Bank of Japan, in remarks for a 2012 conference, noted that the nation was very slow to wake up to the implications of a falling fertility rate which was evident by 1992. "To a significant extent, the decline in growth rates and deterioration in fiscal conditions are attributable to a failure to adjust to the rapid change in demographics," she said. "The implications of population aging and decline are also very profound, as they contribute to a decline in growth potential, a deterioration in the fiscal balance, and a fall in housing prices."

Professor Paul Krugman, in remarks made during a discussion with Japanese officials, pointed to the role the nation's demography plays in its current phase of economic stagnation. "I would say that Japan does have some fundamental reasons for why it is hard to raise demand. The demography in Japan is uniquely unfavourable and the working age population is now shrinking at more than 1 per cent a year," Professor Krugman added that Europe and even the US are not far behind.

## What can we do about it?

Economists generally view the economic effects of demographic change as one which can be ameliorated - if not dissipated - through policy changes, the most significant of which are already underway in the industrialised world. First, minimum qualifying ages to receive state pension benefits are rising, limiting the overall cost of provision. In addition, rising retirement ages may have the effect of 'signalling' to an increasingly healthy, older workforce that wage earning is an activity that can go on much longer than had been accepted. Second, measures to increase workforce participation rates of women – a key part of Shinzo Abe's 'Third Arrow' aimed at boosting Japanese growth rates – should help. The Organisation for Economic Cooperation and Development (OECD) concluded in a 2012 study that if male and female workforce participation rates were to converge, GDP across a group of developed nations would rise by 12.4% by 2030[50]. There also remains the possibility that technological innovation may boost output per worker in ways that are currently unforeseen. Britain is not alone in struggling to understand why productivity growth post-2008 has been much slower than trend growth before the recession.

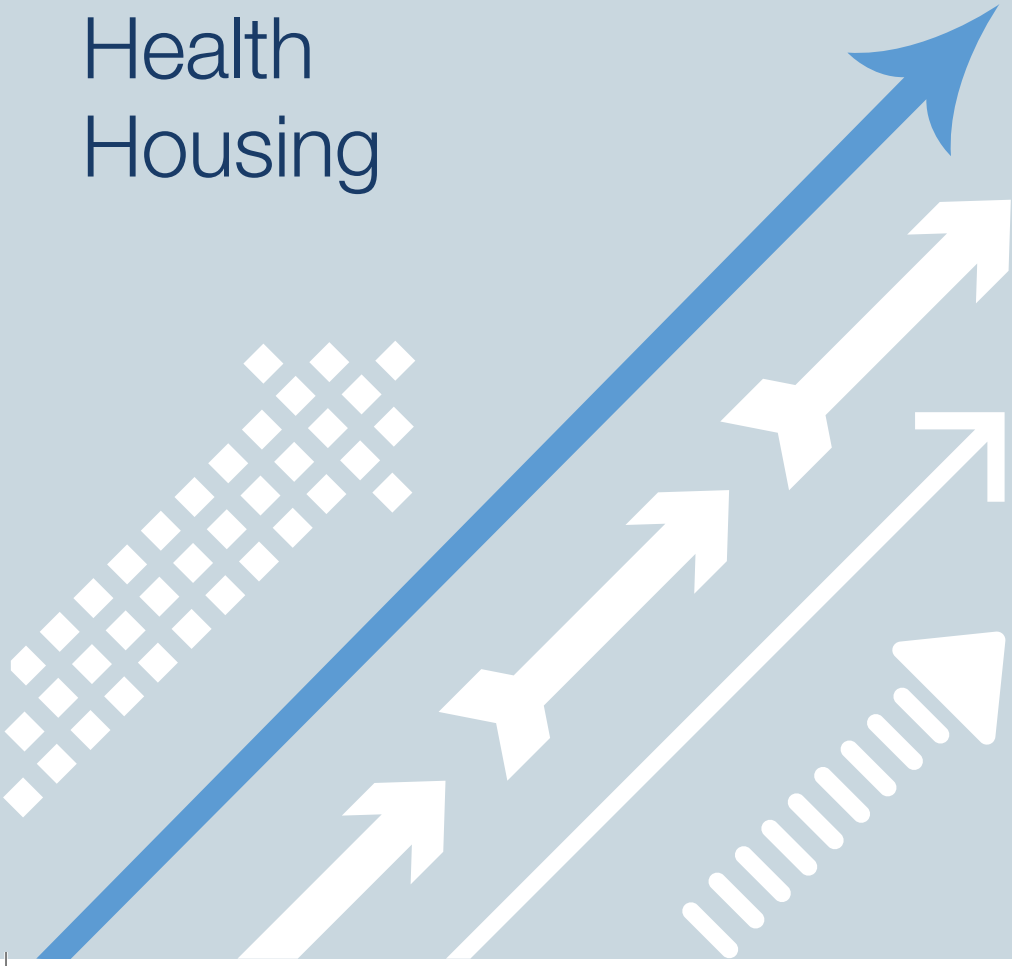
[50] OECD (2012), "Closing the Gender Gap: Act Now", OECD Publishing

But taking advantage of these levers requires structural changes. Simply relying on rising State Pension Ages (SPA) to boost workforce participation rates presumes that labour markets are sufficiently flexible to accommodate an increase in the number of older workers. And although Britain has one of the most flexible labour markets in Europe, underlying data suggest structural impediments to work among older adults. The number of those out of work and over 50 is smaller than that for other age groups but the percentage of these who are long-term unemployed – seeking work for 12 months or longer – is a much higher percentage of the total unemployed. And the percentage of those who have simply dropped out of the workforce in the 50 to 64-year-old category is far higher than at other ages. There are no guarantees that raising SPA translates into a much larger workforce.

Even if policy changes do result in rising workforce participation rates and higher per-worker productivity, policy makers remain stuck with what is perhaps a much larger and complex problem. That is, much of the developed world is producing too few babies to even keep the population stable. Even if human life spans reach a maximum biological level and cease rising – and there is no evidence that such a barrier exists – the available 'store' of new workers and consumers will continue to rise slowly, perhaps too slowly to achieve any discernible level of economic growth. And then what?

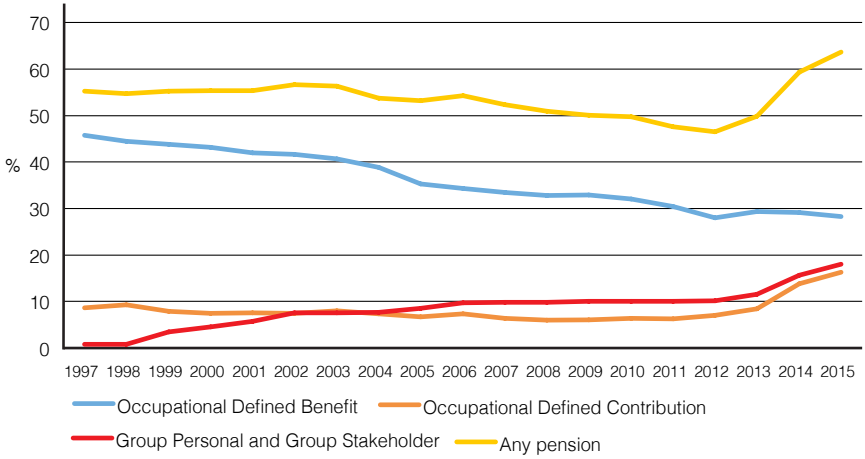
# **Part 3:** Developing coping mechanisms in the face of population change:

Pensions
Labour market
Education
Health
Housing



# Pensions

## Proportion of employees with workplace pensions: by type (1997-2015)



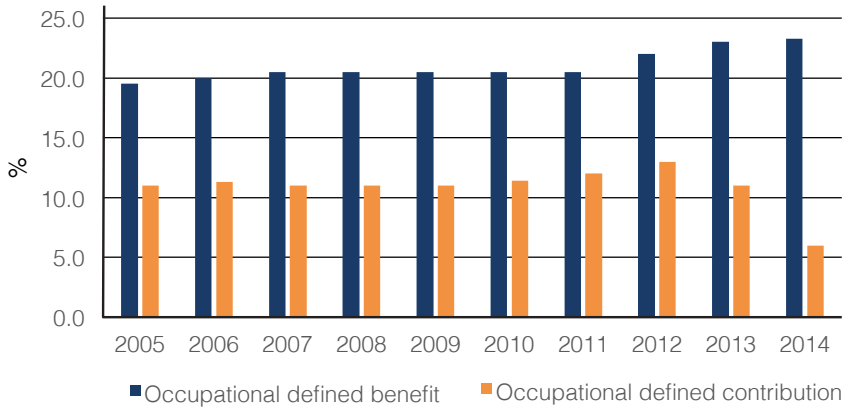

Source: ONS – Annual Survey of Hours and Earnings Pension Tables: 2015 Provisional and 2014 Revised results.

**Between 1997-2015**, the proportion of employees that had a defined **benefit pension scheme fell from 44.5% to 28.3%.**

**Between 2013-2015**, the proportion of employees with an **occupational defined contribution scheme rose from 8.4% to 16.3%.**

**Between 2012-2015**, the total proportion of employees with a **workplace pension scheme has increased from a low of 46.5% to 63.6%.**

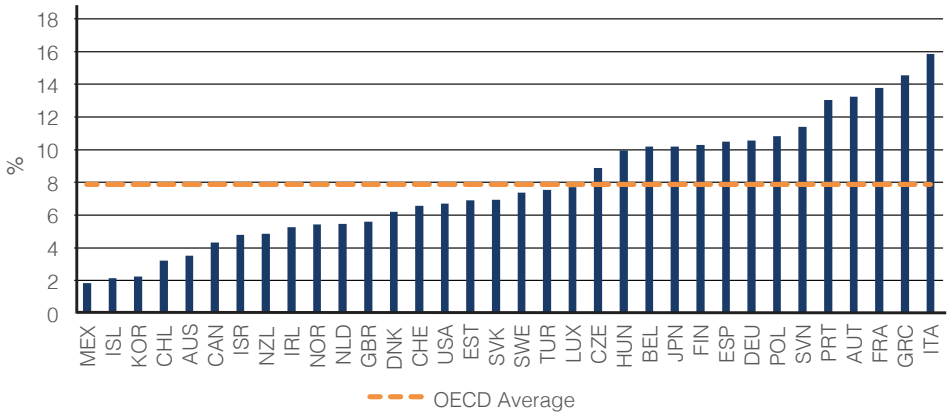
## Total median contribution rates by pension type (all sectors)




Source: ONS – Annual Survey of Hours and Earnings

**In 2014,** the median contribution rate for **defined benefit schemes was 23.3%** compared to only **6% for defined contribution schemes**.

## Public pension expenditure % of GDP




Source: OECD

# Economic-financial literacy for sustainable welfare reforms

Professor Elsa Fornero, University of Turin, CeRP, IZA and Netspar

## Reforms are not mere "technical remedies"

Serious difficulties have emerged over the last quarter of a century in the European Welfare State and in particular in its most important programme, the Pension System. While in public debates these difficulties are sometimes described as a possibly terminal crisis, the need for sustainable welfare programmes continues to be well recognised in Europe as well as all over the world[51]. It is also generally recognized that the answer lies in *structural reforms* capable of responding to profound demographic, economic and social transformations[52].

To be effective and sustainable, and thus able to save the European social model, reforms require people's involvement and *de facto* endorsement. Prerequisites of this are truthful information and understanding of the reforms' basic principles and mechanisms. While this is true in general, it is even more so for reforms that profoundly affect individuals' present and future life, as is the case with comprehensive reforms of the welfare system.

A new paradigm is thus necessary, based on three building blocks: *reforms, information and education*. I have learned this from my academic activity but even more so from my direct experience as Italian Minister of Labour and Social Policies (November 2011 - April 2013), in charge of the pension and labor market reforms, in the technocratic government led by Mario Monti[53].

[51] Huber E. and J.D. Stephens (2001), Development and Crisis of the Welfare State: Parties and Policies in Global Markets, University of Chicago Press.
[52] Barr, N. and P. Diamond (2008), Reforming Pensions: Principles and Policy Choices, Oxford University Press, Oxford. Lindbeck A. and M. Persson (2003), The Gains from Pension Reform, *Journal of Economic Literature*, Vol. 41(1), pp. 74–112.
[53] Fornero, E. (2013), Reforming Labor Markets: Reflections of an Economist Who (Unexpectedly) Became the Italian Minister of Labor, *IZA Journal of European Labor Studies*, Vol. 2(20).

## Rewriting the intergenerational contract: scope and role of pension reforms

For a better understanding of why welfare systems need reforms it is useful to start from a (very stylized) description of their main characteristics, both the good and bad.

Over the course of the 20th century, European countries have been able, mainly through their *welfare* systems, to substantially reduce material deprivation and prevent poverty among older cohorts, whose most important income source has become the public pension. Gradually, they have also become committed to the idea that pensions should consist of guaranteed, stable and generous payouts at relatively young ages.

The system has typically been financed on a pay-as-you-go (PayGo) basis, with revenues (contributions on wages and other labour incomes) directly used, year-by-year, to pay for pensions, with little or no accumulation of funds and often with a top-up from the public budget to cover the annual deficit. Underlying this seeming "*tax and transfer*" mechanism there is an "*intergenerational contract*": the young/active population pays for the current retirees and expects the same will apply when they will be retired, as in a chain-letter mechanism.

An associated Defined Benefit (DB) formula typically granted pension income based on a predetermined proportion of an individual's final earnings, thus making life cycle planning much more comfortable for the prospective pensioner. This pension was then indexed to average salary, allowing retirees' standard of living to keep pace with workers' increasing income level. The formula could be made even more generous when combined with a mere "seniority" exit requirement (i.e. a number of years of contributions, irrespective of age).

These attractive features, however, were not free. They were the result of "liberal" laws, applied to an entire cohort or to specific groups, usually motivated by reference to some kind of "social protection" functions. They were also the result of policy makers' confidence in their ability to act systematically better than an appropriate mathematical formula, more respondent to budget constraints.

The system worked to everybody's satisfaction in times of both demographic and economic expansion: an increasing number of young workers were able to

pay for their parents'-grandparents' pensions with their paychecks on a sharply increasing trend because of economic booms and increasing productivity. When these favorable conditions waned, shortsightedness took the place of enthusiasm and it was considered feasible to continue to operate the system although the essential conditions were no longer there.

This political game was reinforced by the demographic transition which steadily increased the *median voter's* age, giving a decisive electoral weight to older cohorts[54]. The DB formula could be used to meet the expectations of the most prominent pressure groups (high bureaucrats, managers and public employees, not to mention politicians themselves), ending up in socially unacceptable "gifts" being graciously presented to them on retirement day in the form of sometimes unwarranted large pension checks.

All this contributed to a general social and political climate in which attention shifted from the insurance/saving principles of a pension scheme to entitlements (or "acquired rights", considered unalterable), with little consideration, if at all, for "*who pays the price*". The system progressively became not only financially untenable but also more and more opaque, with large and small groups of workers scrambling for some privileges. As societies aged, it resulted in a huge and increasing "*pension debt*" (the net value of future pension entitlement translated in today's money), which was often much larger than the "explicit" public debt. Their combination, against the background of fast-ageing societies and sluggish productivity, left younger workers - and their dwindling offspring – with the impossible burden of paying "generous" benefits to a fast-growing number of early retirees who lived ever longer (where generosity refers of course not to the absolute amount of benefits, but to the proportion paid by own contributions).

European countries had little choice but to redesign the systems – or face sovereign bankruptcy. In principle, it would have been wiser to introduce reforms during a period of steady growth, when sacrifices would have been more easily acceptable than at times of recession: it is easier to reduce the slices of a growing pie than of a shrinking one. It lies however in the nature of electoral politics that political parties will be reluctant to "spoil" present good times by introducing painful reforms designed to prevent future problems[55]. This

[54] Galasso V., (2006), The Political Future of Social Security in Aging Societies", 2006, The MIT Press
[55] As Jean-Claude Juncker's once said: "*We all know what to do, but we don't know how to get re-elected*

is why reforms are usually introduced in difficult times, if not in an emergency[56].

## A new notion of "reform"

Reforms have both a technical and a political side. From a *technical* point of view, research has reached a relative convergence towards a prevalent "insurance view" of pension programs, based on an analysis of both individual and macro risks, in order to respond more efficiently to their changes across generations, age and gender. Requirements for a "good" pension system have shaped policy discussions and determined, at least partially, the course of reforms in Europe. These include:

- a *mixed system,* partly public and PayGo and partly private and funded, based on financial markets' returns. Feasibility considerations recommend limited and gradual funding because even a partial transition from PayGo to funding raises important financing problems that risk jeopardizing the result. In this regard, the PayGo has to be more balanced towards young and future cohorts. A greater correlation, at the individual level, between contributions and pensions can serve the purpose. The combination of "*notional*" *funding* with a Defined Contribution formula[57] makes it possible to tailor pension benefits to individual workers' contributions without actually having to capitalise and invest the sums paid in. Each worker has their own pension account, where all contributions paid in their name are reported, summed up, and rewarded at a rate of return that, for the system to be balanced, must be (approximately) equal to the national income (or wage bill) growth rate. At retirement, which can occur within a given age range, an actuarial factor, taking expected longevity at retirement into account, can be applied to determine the initial benefit.

- An automatic adjustment of retirement ages to longevity (i.e. life expectancy at the beginning of the pension period) helps avoid the social tensions that usually accompany parametric changes of the system, provided the quality of life of the extra years is good and the increase in longevity is somehow split between

*once we have done it*". The Economist, The Quest for Prosperity, 15 March 2007.

[56]In the early 2000s, Germany was able to implement effective pension and labor market reforms, after having become "*the sick man of Europe*" and not without political cost: Chancellor Gerhard Schroeder lost his job in the 2005 elections. Nearly a decade later, Italy, Spain, Greece and Portugal had to push through pension and labor market reforms in much stormier economic times. Understandably, both the sacrifices required from the people and the political upheaval were far greater, as was resentment against "austerity".

[57] the so called NDC system, see: Holzmann R and Palmer E., eds., (2012), Nonfinancial Defined Contribution Pension Schemes in a Changing Pension World, Volume 1: Progress, Lessons, and Implementation, The World Bank, Washington DC.

working life and retirement.

- Solidarity, in the form of explicit tax-financed exceptions, directed at workers who could not reach an acceptable retirement income during their working lives, has to continue to be part of a public pension scheme while transparency and more uniform rules (with exceptions directed, as just said, at less fortunate workers) should reduce privileges.

**The paradigm "Reform, Inform, and Educate" as an alternative to both paternalism and populism**

Reforms, however, are not academic exercises and not mere technical problems. They necessarily include a political angle inasmuch as they change people's expectations and life plans and must receive not only formal consensus in Parliament but also basic consensus from the population at large. Should this basic consensus be lacking, the reform will be met with hostility and run the risk of being either formally reversed or practically disregarded.

Conditions for practical success of a pension reform must therefore include the reform's capability to provoke a shift in attitudes and behaviour. Those of us who are middle-aged (or above) are enjoying (collectively) an almost unprecedented concentration of wealth (including generous pension entitlements), privileges and political power. This concentration has left many younger people with a much smaller range of lifetime options than their parents. In many European countries, unemployment rates for younger people are twice or three times higher than for more senior workers.

The demographic transition therefore represents a very serious challenge to society not only because of shrinking labour forces but also in terms of income distribution and of perspectives offered to younger people. All this implies that social security reforms cannot be entrusted to a cluster of specialists, such as economists, lawyers and actuaries. The concept of reform must become much more comprehensive, and encompass three different dimensions, of which the reform is just one and not the most difficult.

**i. Reform.** The reform process has to be completed, according to consistent insurance principles, coupled with a fair amount of transparent income redistribution in the right direction, i.e. from richer to poorer, and not vice versa. Adequate old age insurance, inclusive not only of retirement income but also of Long-Term Care in old age, requires individuals to be safeguarded against

both adverse general economic conditions (such as the Great Recession) and personal misfortunes affecting their pre-active and active life such as lack of education, unemployment, sickness, and invalidity. The welfare system cannot be separated from the macro economy. At the end of eight years of downright recession or abnormally low growth, the time has come for a soberer analysis on the links between the pension system and the labour market. Dynamic and inclusive labour markets, that make it easier for workers to find a job and for employers to hire and fire, are the best prerequisite for adequate pension systems. Long-term employment-enhancing policies, such as apprenticeship and lifelong learning, must be given greater importance and more resources.

On top of everything, it should be recalled that economic growth remains the major force supporting both the adequacy and the long run stability of a PayGo system. Since it creates additional jobs, growth at suitable rates tends to strengthen the association between being in *active age (20-64)* and being *employed*, by reducing unemployment and encouraging labour force participation (through reduced incentives to early retirement or to homemaking). Unfortunately, since the early 1990s, the rate of growth of productivity has slowed in Europe and the US. With constant or declining population, per capita income growth should regain its centrality in supporting welfare.

**ii. Inform**. The accumulation of pension wealth is a long and complex process. Workers must have an idea, as precise as possible, of where they stand on pension wealth and retirement options so that they can make the sensible personal retirement choices the reforms require from them: first, whether to retire early, on a comparatively low pension or to stay in work longer aiming for a higher, although further away pension. And, second, how to make sensible general decisions on how the funded part of their pension wealth should be invested by pension funds. This knowledge should help them to avoid mistakes and disappointments such as shortfalls of actual versus expected retirement income and ensuing painful lifestyle adjustments.

**iii. Educate.** While information is essential, *per se* it is not enough. People have to be able to understand. Information thus has to be integrated with Economic Financial Literacy (EFL), not as a basis for abstract knowledge but as another essential part of pension reforms. Without the EFL-information mix, the fundamentals for the reforms' political sustainability are clearly at risk. In spite of their essential role, both information and EFL are very poor. Statistical surveys

have shown widespread financial illiteracy as well as information gaps[58]; research has shown the importance of such literacy[59].

Some fundamentals of EFL should be here summarily remembered: a) the notion of compound interest - in no way intuitive or easy for people with only a light arithmetical background - is crucial to the understanding of how pension wealth accumulation works; b) the core concept of risk diversification is a good preliminary concept for rational decisions about participating in pension funds or, more generally, in considering the different risk–return combinations of an unfunded and a funded pension scheme; c) elementary knowledge about money flows and its instruments (from credit and debit cards to bank accounts) is rapidly becoming essential for the ordinary citizen; d) some very general knowledge about national income accounts, taxation and public sector accounts appears to be a necessary complement to the predominantly individualistic approach of most popular financial literature and education programs. EFL should accompany individuals throughout their educational period and become a constant element of their adult life. The depth and complexity of this knowledge may, of course, vary considerably according to their study curriculum and their profession.

A general increase in EFL (even on a very large scale) cannot, of course, be the successful answer to all economic and financial problems; it would be naive to think so, particularly as empirical evidence has yet to be provided to support the hypothesis of a direct correlation between EFL and the effectiveness of reforms. “Nudges” can still encourage even economically and financially literate people to make “wise” choices[60]. EFL appears, however, a substitute to be preferred to both populism and paternalism.

[58] Lusardi, A. and O. S. Mitchell (2011), Financial Literacy around the World. An Overview, *Journal of Pension Economics and Finance*, Vol. 10(4), pp. 497–508

[59] Lusardi, A. and O. S. Mitchell (2014), The Economic Importance of Financial Literacy: Theory and Evidence, *Journal of Economic Literature*, Vol. 52(1), pp. 5–44.

[60] Thaler, R. H. and C. R. Sunstein (2008), Nudge: Improving Decisions about Health, Wealth and Happiness, Yale University Press, New Haven

# What sorts of pensions and savings delivery models are likely to be viable and fair across generations?

Steve Webb, Director of Policy, Royal London and former Minister for Pensions, 2010-15

The big challenge for policymakers in an area such as pensions and long-term savings is coming up with a delivery model that will stand the test of time. Far too often in the past a government has designed a system of retirement provision only to see it ripped up and replaced within a decade. For both workers and employers, this constant change undermines confidence and engagement in pension saving. But with the raft of reforms implemented in the last five years there is finally the chance of a stable and sustainable regime for retirement saving.

Going back to the late 1970s, there was a very clear vision for how retirement saving was to work. In 1978, a new state earnings-related pension scheme (SERPS) was introduced, with a view to delivering generous earnings-related pensions to workers who did not have access to high quality occupational pension schemes. The combination of a Basic State Pension uprated relatively generously each year and a comprehensive earnings-related state top-up would have given many workers a good level of security in retirement.

The problem with that model was that it was heavily dependent on unfunded State Pension promises. The workers of the 1970s, 1980s and 1990s were essentially promising themselves generous state pensions which would be paid for by the National Insurance Contributions of their children. With an ageing population and a declining birth rate, this represented a huge unfunded claim on the tax base of the next generation.

This settlement lasted less than a decade. As early as 1980 the link between State Pension upratings and average earnings was broken (not to be restored for thirty years) and in the mid-1980s legislation was introduced which roughly

halved the generosity of the SERPS scheme. Further legislation in the mid-1990s saw further cuts in the value of rights under SERPS.

The 1980s also saw a move towards private pension provision with the ability of people to opt out of the state scheme not only into traditional salary-related occupational pensions but also into new 'money purchase' defined contribution arrangements. Under these schemes, individuals and their firms would contribute into a fund which would be invested and used at retirement to buy an annuity or income for life. At the time, a combination of relatively buoyant investment returns and increasingly generous taxpayer incentives led to several million people taking out personal pensions of this sort.

However, after the original surge of enthusiasm for personal pensions, problems began to emerge. It became clear that many people had been 'mis-sold' personal pensions, giving up valuable occupational pension rights simply to chase a short-term government incentive or because of pressure from a salesman. It also became clear that this reform had not addressed the long-term decline in coverage of workplace pensions. Employers were increasingly starting to restrict access to salary-related workplace pensions and few workers were actively "opting in" to pension saving.

The post 1997 Labour government experimented with the concept of 'stakeholder pensions' – charge capped, standardised products that had to be made available in all workplaces beyond a minimum size. But apart from a brief uptick in interest, the stakeholder experiment failed and the long-term decline in workplace pension coverage continued. By 2010 barely one worker in three in the private sector had any workplace pension provision at all.

It was clear at this point that a new settlement was needed, which would re-define the role of the state, the employer and the individual and which would overcome the inertia which led many not to engage with pension saving at all. The reform programme of the 2010-15 government therefore sought to develop a new model, building in some important respects on the excellent work of the Pensions Commission headed by Lord Turner.

**The first thing to sort out was the state pension.**

Thirty years of being linked to price inflation meant that the value of the Basic State Pension had fallen to record low levels relative to average wages. Millions of pensioners were receiving means-tested top-ups through pension credit,

housing benefit and other benefits, because their state and private pension incomes were simply not enough to live on. Whilst the last government had no fiscal room for manoeuvre (indeed was trying to tackle a large budget deficit) it was still necessary to devise a new State Pension infrastructure.

The Coalition legislated for a new 'Single Tier' State Pension from April 2016 to take the place of the two-tier system of a Basic State Pension and a SERPS pension (with complex 'contracting out' arrangements for workers in occupational schemes). In the early decades of the reform the new system will cost broadly the same as the system that it replaced, but more and more people will get the 'flat rate amount' (currently around £8,000 pa) rather than a variable amount based on past earnings. The idea of the new system is to increase the predictability of State Pension outcomes and to get people to a bare subsistence minimum – just enough to live on. The new system was not opposed when it went through Parliament and is likely to form the basis of a simpler and more certain outcome for retirement saving for years to come.

However, given that the new flat rate is probably only around one third of the national average wage, most workers will want and need additional pension provision.

The second key reform therefore was the implementation of the system of automatic enrolment, first proposed for the UK by the Turner Commission. A lot of detailed work was done to improve the legislative framework but the programme was successfully launched in late 2012, starting with the largest employers.

With one caveat, it has been a huge success. At time of writing (Spring 2016) nearly six million workers have been enrolled by their employer into a workplace pension and less than one in ten has exercised their right to opt out. The staging of employers into automatic enrolment continues over the coming two years but by the end around ten million workers will have been enrolled and the vast majority will now be building up a private pension of their own to complement their State Pension rights.

The biggest caveat is that the amounts going in remain tiny. So as to ease the transition to the new system, the mandatory minimum contribution rate from employers and employees starts at a combined 2% of a band of 'qualifying earnings', rising to 5% in April 2018 and 8% in April 2019. Whilst this is a

hugely welcome start, it does mean that most individuals currently have tiny automatic enrolment pension pots. For example, at the time of writing whilst there are more than 2.5 million members of the government's flagship not-for-profit NEST pension scheme, the average pot is less than £300 per head. For automatic enrolment to be truly successful, we urgently need agreement on how to proceed once the 8% contribution rate has been achieved. My personal preference would be a system of 'automatic escalation' (as widely operated in the US) where individuals pre-commit that part of any future pay rise will go to increasing the rate of pension contributions.

Whilst automatic enrolment was generating positive headlines, the fact that most people had to turn their workplace pension pot into an annuity at retirement was generating negative headlines. A combination of increased longevity and record low interest rates (owing in large part to macroeconomic policy) meant that each cohort of newly-retired savers was getting less and less for their pension pot. There was a danger that this would fundamentally undermine the attractiveness of pension saving in general and automatic enrolment in particular.

As a result, in 2014 the Government announced it would give people 'freedom and choice' over how they used their accumulated pension pot. Instead of the presumption that most people would buy an annuity, people would instead be free to use their pension pot as they saw fit. If they wanted to take the whole lot as cash then, subject to the requisite taxation, they could do so. If they wanted to go on investing whilst drawing an income, they could do so. If they wanted to mix and match, taking some taxed cash and some tax free cash they could do so. This revolution freed up millions of people from the requirement to take an annuity and has made pension saving a far more interesting and popular idea.

Although the reforms were controversial at the time, with fears that people would 'run out' of money before the end of their life, the general response seems to have been measured and positive, with most people cashing in only relatively modest pots (e.g. around £15,000) and others using the opportunity to go on investing for longer. It is hard to see that these new freedoms will now be reversed, though it is possible to imagine some tighter regulation on some aspects of the process.

But one further change was needed to make pension policy sustainable

– action on the State Pension Age. Under the timetable set out in the 1995 Pension Act, male and female pension ages were to be progressively equalised over a decade starting from 2010. Women's pension ages were to be gradually stepped up from 60 in 2010 to 61 in 2012, 62 in 2014 and so forth to 65 in 2020. The problem was that this would still leave male state pension ages in 2020 at the same level as they were nearly a century earlier, despite huge growth in life expectancy. This would have placed an unacceptable burden on the next generation of workers who would have faced ever-increasing tax and NIC bills to pay for the unfunded State Pensions of older generations.

As a result, the last government legislated in 2011 to bring forward the date at which equality at 65 was reached, from 2020 to 2018, and then to reach equality at 66 in 2020 and 67 by 2028. This legislation added twelve months to the working lives of most of those affected but did add up to 18 months to the pension ages of a smaller group, especially those born in early 1954. This group had already faced an increase of more than four years in their pension age under the 1995 Act, so the combined effect was substantial, especially as not all were aware of the provisions of the 1995 Act.

In order to make future changes more systematic, the 2014 Pensions Act provided for a five-yearly review of State Pension ages, and the first has just been launched. The idea is to learn from the past. Instead of leaving pension ages alone for decades while longevity surges ahead, five-yearly reviews will mean that realistic pension ages can be maintained on an ongoing basis. The principle behind the reviews is intended to be that we should all spend around two thirds of our adult life "in work" (or more precisely, 'below state pension age') and one third "in retirement" (ie 'over state pension age). This is designed to avoid sudden increases in State Pension ages at short notice and also to avoid future generations of workers facing unsustainable bills for today's retired population.

The model we have now reached therefore is a carefully planned and coherent one which has a chance of standing the test of time. We have a single headline State Pension rate which will increasingly become the norm for those coming up to retirement and will allow people to plan with certainty. We have mass membership of well-regulated workplace pensions through automatic enrolment, where the worker and the firm combine to build up a second pension for each worker earning above a threshold figure. And we have

greater 'freedom and choice' for individuals to tailor their choices at and around retirement. But we still have to address the fundamental question of adequacy, with millions still not saving enough.

We have a good framework which has the potential to be with us for years to come. We now need to get the incentives right, to ensure that each individual builds up a large enough pension pot to give them real choices in retirement.

# Avoiding lemons: The UK workplace pensions challenge[61]

Gregg McClymont, Head of Retirement Savings Aberdeen Asset Management and Former Shadow Minister for Pensions and Andy Tarrant, Head of Policy, the People's Pension[62]

## Introduction

The American economist George Akerlof won the Nobel prize in 2001 for his paper *The Market for Lemons*[63]. The paper analysed the consequences of information asymmetries in the second hand car market. The greater knowledge possessed by sellers led to buyers purchasing 'lemons' – poor value used cars. Akerlof emphasised the wider applicability of his study: in markets where sellers possess much greater information than buyers, poor quality goods will inevitably drive out good ones. The market will become dominated by sellers of poor quality goods and the number of buyers will drop dramatically in response. Institutions acting as guarantors of quality are the necessary antidote to such market failure.

The UK is in the midst of major reforms of pensions. The Basic State Pension and the earnings-related additional state pension scheme are being merged into a single flat-rate State Pension. The intention is to create a foundation pension on top of which people will build workplace private pension provision. The foundation pension's value is likely to be approximately £7800 per annum. This is roughly 30% of the average wage. Thus a replacement rate that provides a reasonable standard of living in retirement requires significant additional workplace private pensions saving.

Achieving value for money workplace private pensions means keeping 'lemons' at bay. This is a challenge: this is a market which features not just

[61] A version of this essay appeared in Towards a New Pension Settlement (Rowman and Littlefield and Policy Network, 2016).
[62] This chapter represents the personal views of the authors alone.
[63] Akerlof, A.G. "The Market for "Lemons": Quality Uncertainty and the Market Mechanism" *The Quarterly Journal of Economics*, Vol. 84, No. 3. (Aug., 1970), pp. 488-500.

major information asymmetries[64] but also a new twist on the principal-agent problem – the ultimate consumers, employees, do not choose the product, employers do so. The individual – even if aware of product deficiencies – is unable to switch for this reason; more widely the principal-agent problem manifests itself via smaller employers, who do not have the time or expertise to monitor pension quality. This is why the Department of Work and Pensions found in a 2012 survey of workplace pension schemes that 59% of employers running smaller contract-based schemes (sized between 12 and 99 members) did not know that their employees paid any pensions charges at all[65].

If common sense dictates 'the market where possible, the state where necessary', then workplace pensions, for the structural reasons examined above, necessitate government oversight. All British employees are being auto-enrolled into workplace private pensions. If 'lemons' flourish, Akerlof's insights tell us that mass opt-outs will eventually follow.

The UK workplace private pension market is characterised by a sharp decline in traditional defined benefit (DB) pension schemes. Most employers do not want to carry the substantial investment risk and actuarial risk onto their balance sheet. The number of workers in private sector DB schemes still open to new members is just 1 million; the total private sector workforce is 23 million. The provision of workplace pensions is now largely via defined contribution (DC) schemes. These pensions, unlike DB, offer no guaranteed income. Instead, retirement income depends on the performance of the funds invested. Before auto-enrolment, the providers of DC pensions had managed to persuade only a small and declining number of savers – about 900,000 – that it was worth investing in these products[66]. The state is now requiring employers to purchase these products on behalf of potentially 10 million people[67].

Semi-compulsion for pension saving (auto-enrolment) was adopted because successive governments recognised the behavioural barriers to pension saving. The behavioural barriers are such that when the vast majority of pension savers are auto-enrolled, they elect to make no active choice but save into the

[64] Not least the one-off nature of consumption which removes learning by doing until it is too late.
[65] DWP, Pension landscape and charging: Quantitative and qualitative research with employers and pension providers, 2012
[66] http://www.ons.gov.uk/ons/dcp171766_313466.pdf,p.9
[67] https://www.gov.uk/government/news/standing-ovation-as-auto-enrolment-hits-5-million-and-auto-transfer-launch-plans-are-unveiled

default scheme offered by the pension provider. This has always been the case – historically, around 80-90 per cent of savers into pre-auto enrolment trust-based company DC schemes also made no active choice as to the funds in which they would be invested but were instead allocated to the default option, monitored by trustees.

## The potential 'lemon' characteristics of british pensions are:

### A lack of transparency of costs and charges

Historically, pension providers have not disclosed all their costs and charges, large numbers of pensions were sold with high charges,[68] absorbing too much of the investment gains. The result for savers was smaller pension pots and reduced retirement incomes[69]. Under pressure from a coalition of consumer groups, employee representatives and the official Opposition the government introduced an annual management charge cap of 0.75% or the default option in pension schemes. But the government has not applied this cap to the substantial pensions savings left behind by employees when they switched jobs prior to the price-cap coming into effect– known as 'stranded pots'. The same pro-consumer coalition also campaigned for transparency of the costs incurred by the fund managers[70] with whom pension schemes invested pension contributions (often within vertically integrated companies). Again, the government conceded that these should in principle be declared. The Financial Conduct Authority (FCA) is currently consulting on which costs should be declared and it remains to be seen whether effective transparency will be achieved.

### Lack of scale

Pension schemes in the UK are typically organised around an individual employer. This means that most forgo the economies of scale that would significantly reduce administrative overheads, and increase investment and, therefore, member returns. There is however scale on the seller side. The DC market is dominated by a small number of insurance companies increasingly

[68] A third of pension savings are in schemes charging above 1% according to the FCA (2014) report "Defined contribution workplace pensions: The audit of charges and benefits in legacy schemes". Logically, the audit should actually have covered all savings being charged more than 0.75%.
[69] The OFT estimated that a 1% annual management charge would reduce retirement savings for someone on an average salary by 21% http://webarchive.nationalarchives.gov.uk/20140402142426/http:/www.oft.gov.uk/shared_oft/market-studies/oft1505,p.71.
[70] These are separate from the annual management charges of the pension scheme.

selling group personal pensions (GPPs), although mastertrusts are growing too in the auto-enrolment space and now serve over 6 million members, their assets under management are dwarfed by the insurers[71]. GPPs enable price discrimination between the employees of larger and smaller employers. There are currently about 140,000 DC pension schemes in the UK.[72].

### Inadequate governance

Traditional DB schemes should be aligned with the interests of their members because they have trustees who are legally required to make all of the decisions about the scheme and to do so prioritising the interests of the members above all others. Contract DC providers have to take the savers' interest into 'account' but are legally obliged to prioritise their shareholders. In a market without extensive information asymmetries, buy-side pressure would normally serve to align shareholder and member interests. Insurance companies do provide trust-based DC schemes where employers request them. However, such provision needs to be universally available. Faced with consumer groups and Labour party complaint as to the inadequate nature of DC governance, the last government opted instead to require contract-based providers to install 'independent governance committees'. Conflicts of interest are permitted on these bodies, which are appointed by the pension provider and which are advisory rather than governing.[73]

### Inadequate regulation

Trust-based pension schemes are regulated by the Pensions Regulator (TPR). Contract-based schemes are regulated by the FCA. In short, their respective approaches could be summarised as follows. TPR prioritises the savers' interest but has inadequate powers, the FCA has adequate powers but is relying on heretofore absent buy-side pressure to drive product improvement.[74]

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71 http://www.ftadviser.com/2016/05/23/pensions/the-people-s-pension-overtakes-nest-as-biggest-ae-scheme-eA1OMrnXsB78DA1ATWzvyM/article.html; https://www.abi.org.uk/Insurance-and-savings/Products/Pensions/Saving-into-a-pension/ABI-life-and-pension-funds-the-ABI-sectors

72 www.ftadviser.com/2016/05/23/pensions/the-people-s-pension-overtakes-nest-as-biggest-ae-scheme-eA1OMrnXsB78DA1ATWzvyM/article.html; https://www.abi.org.uk/Insurance-and-savings/Products/Pensions/Saving-into-a-pension/ABI-life-and-pension-funds-the-ABI-sectors

73 The Labour Party's Shadow Pensions Team in the 2010-15 Parliament provided detailed comments on governance design to the OFT and the FCA. Please contact andy_tarrant@yahoo.com if you would like to obtain copies.

74 For a longer discussion, see http://henrytapper.com/2015/07/07/the-future-of-pension-regulation-an-drew-tarrant/

## Retirement income free-for-all

The market for annuities provides a good example of the FCA approach. Until last year, retirees had to purchase an annuity with the savings pot they had built in a DC pension scheme. (An annuity is a regular income stream purchased with a lump sum formed from the pension savings accumulated prior to retirement). However, inertia characterised the behaviour of a large proportion of savers and they were channelled into buying annuities directly from the pension provider with whom they saved, without first considering all the offers on the market. The consequence of this was an income in retirement which was often 20% below what could have been achieved[75]. The FCA approach was to increase the prompts given to savers rather than ensure that savers were offered the best product available.

The unpopularity of annuities generated a political reaction. The government legislated to lift the requirement to purchase them. However, this does not remove the existence of longevity risk (i.e. the risk that you may live longer than you expect and therefore run out of savings) and therefore the need for an annuity or annuity-type product at some point in retirement. So annuities still require effective regulation.

The majority of purchases will now be of income drawdown products where the savers pension pot stays invested and a mixture of profit and capital is withdrawn to provide income. All of the 'lemon' characteristics described above will now apply to the retirement income phase, but neither the government nor the FCA have any plans to regulate. The FCA is consulting on its regulatory approach to retirement income products in 2016 but consistent with its standard approach, the direction it gives respondees is to answer questions relating to consumer prompts[76].There is now a logical disconnect between the semi-effectively regulated default saving phase and the unregulated retirement income phase. With respect to the latter, the government's approach is to rely on offering savers a non-mandatory short 'guidance' interview to help them with a complex one-off purchase with potentially life-changing implications. The worry must be that many savers will simply buy drawdown products in the same way they purchased annuities. This outcome is hardly what savers say they want from a pension system, which is "pension provision that supports

[75] NAPF (2012) "Savers Left Short-Changed and Bewildered by Unfair Annuities System"
[76] Financial Conduct Authority, (2015) "Pension reforms – proposed changes to our rules and guidance"

members' best interests without requiring active customer choice"[77].

### No system to direct employers to schemes with high quality default products

There is no licensing system for workplace pension schemes in the UK. Such a licensing system would be ideal for dealing with asymmetry of information and ensuring a reasonable number of scale, well-governed, low-cost providers, such as NEST, NOW and the Peoples Pension could compete in the market. Employees could be secure in the knowledge that their employer had selected only from pension schemes that meet quality criteria with respect to delivering value for money, including governance criteria. Furthermore, the absence of a licensing scheme is one of the factors which facilitates the pension scammers engaging in fraudulent activity[78].

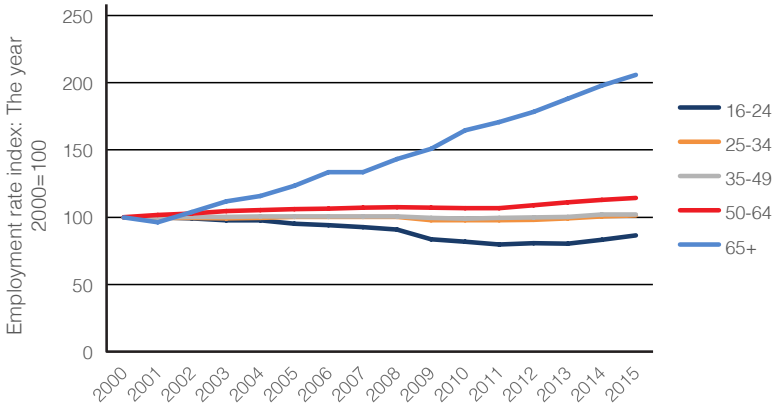
### Conclusion

Auto enrolment has been a major UK policy success. However, its supply-side foundations contain shades of "lemon" and there are obvious reforms which could and should be undertaken to make the foundations robust.

[77] See principle 8 on page 30 of the research into consumer demand in IPPR "Defining ambitions: shaping reform around public attitudes" (2013) p. 33.
[78] Jones, R (2015) "Protect Pensioners from Scammers who want their savings, say MPs", The Guardian, Tuesday 10 March

# The labour market and welfare spending

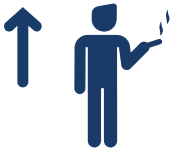
## Employment rate index by age group




Source: ONS – Labour Force Survey and author's calculations

**Between 2000 and 2015,** the employment rate for the **over 65s doubled** according the index constructed using data **from the Labour Force Survey.**

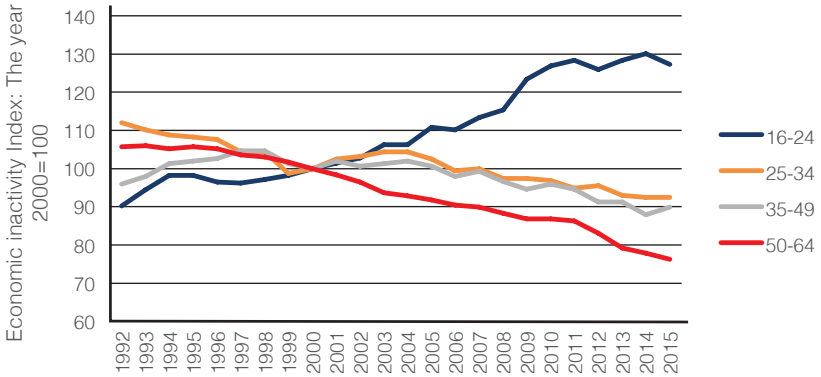
**Over the same period,** employment rates among **16-24 year olds fell.**



**Between 2000 and 2015, economic inactivity rates** among **16-24 year olds increased by a quarter.**

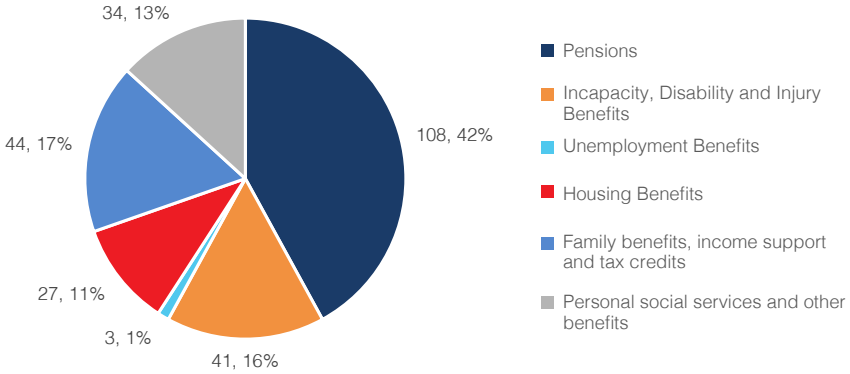
**Economic inactivity amongst older workers** nearing retirement **has been consistently falling. Between 2000 and 2015,** inactivity rates among **50-64 year olds fell by almost a quarter.**

## Economic inactivity rate index by age group




Source: ONS – Labour Force Survey and author's calculations

## Government welfare spending




Source: ONS – Public Sector Finances

**In 2014-2015**, **£108 billion** was spent on pensions, **42% of the entire welfare budget.**

This is **more** than what is spent on **incapacity and disability benefits, unemployment benefits, housing benefits** and **personal social services** combined.

# The welfare state and the young

Professor David N.F. Bell, Division of Economics Stirling Management School, University of Stirling, IZA and CPC

Professor David G. Blanchflower
Department of Economics, Dartmouth College,
Division of Economics, Stirling Management School,
University of Stirling, IZA and NBER

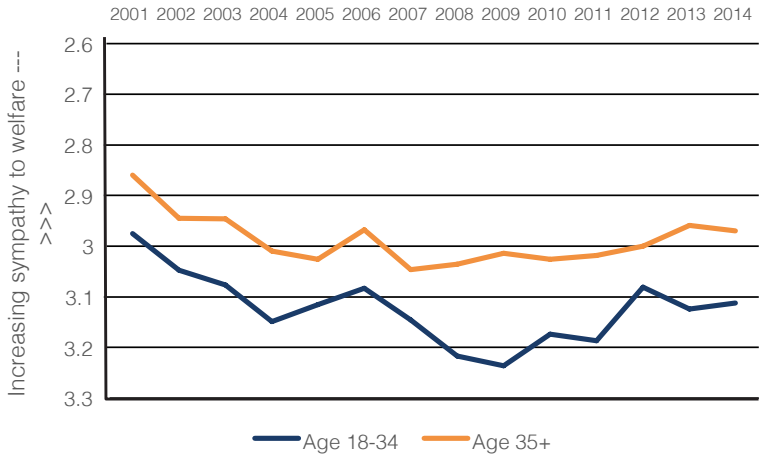
The longevity of Britain's welfare state can only be assured if succeeding generations are willing to support its continuation and are able to provide the necessary resources. Therefore, from the perspective of young people, there is both a political and an economic dimension to maintaining Britain's welfare state. The young will be asked to provide a substantial level of support during the next two decades as Britain's population ages rapidly. They may not be willing, or able, to provide this support.

Our contribution focuses on their ability to provide the resources necessary to maintain Britain's welfare services. Thus we concentrate on the economic challenges facing the young, but first we make one important observation regarding the political economy of the welfare state: it relates to support for its values. We would suggest that the young are less supportive of these values than previous post-war generations. Our evidence is drawn from the "welfarism scale" collected in the British Social Attitudes survey. This scale is constructed by amalgamating responses to questions such as "the welfare state makes people nowadays less willing to look after themselves", "people receiving social security are made to feel like second-class citizens", "the welfare state encourages people to stop helping each other". Responses are combined to form the welfarism scale. Lower scores on the scale indicate attitudes more supportive to welfare.

Figure 1 shows average scores for the period 2001-2014 for those aged up to 35 and those aged 35+. First, it suggests that not only has there been a general fall in support for values supportive of the welfare state, but also that the young are less supportive of these values than are older people. Second, the

gap between young and old was particularly marked at the start of the Great Recession, which may reflect the particular difficulties faced by the young at that time. Third, taking the period as a whole, the gap in attitudes to welfarism between the young and old is certainly not closing and may be increasing. Support for the welfare state among young people cannot be taken for granted: changes in attitudes are likely to eventually be reflected at the ballot box.

**Support for welfare by age group: 2001-2014**




Source: British Social Attitudes Survey

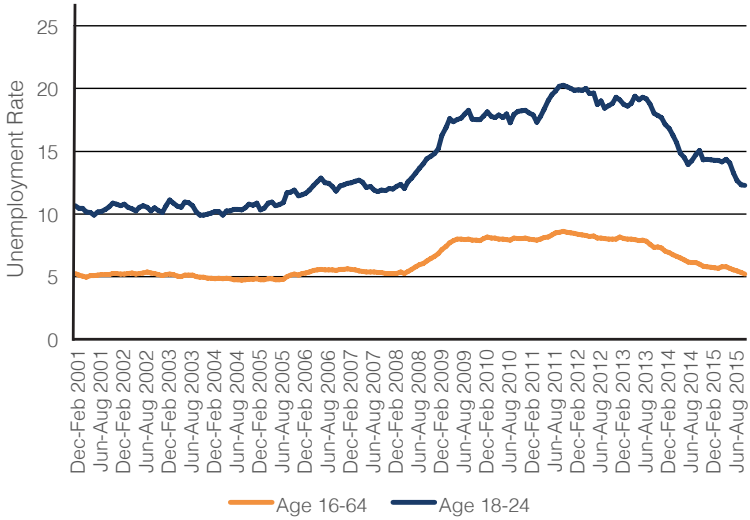
We devote the remainder of our contribution to the question of whether young people will be able to provide the resources needed to support the welfare state. The answer principally depends on their productivity, which in turn is closely linked to how they fare in the labour market. Why does productivity matter? At present, there are 3.25 individuals of working age for each person of State Pension Age in the UK: taking account of changes in the State Pension Age, this ratio will fall to 2.78 by 2036. Workers' productivity will have to increase significantly simply to maintain current levels of support for older people.

Part of the answer to increased productivity must be to find policies that will bring those groups at the margins of the labour market into employment. The Great Recession has had a particularly harsh impact on the labour market prospects of younger people, particularly those who are further marginalised by their ethnicity, race etc. To establish these conclusions, we focus first on jobs and then on wages.

## 1. Youth Joblessness

First consider the chances of the young finding jobs. Youth unemployment rates in the UK are consistently above those of the working age population. They rose above 25% in 2011 in the middle of the Great Recession and, while they have fallen as the British labour market has recovered, they are still significantly higher than adult rates.

**Unemployment rates by age group**




Source: Labour Force Survey

In October 2015, the youth unemployment rate in the UK was 13.5% while in Germany it was 7%. Not only are German youth unemployment rates significantly lower, the ratio of the youth to the adult unemployment rate - a key measure of the integration of young people into the labour market was 1.6 in Germany compared with 2.6 in the UK. The UK fails to match the standards of countries such as Germany with effective mechanisms for introducing young people to the world of work.

Young people from ethnic minorities face even greater difficulties in the labour market. Between April 2014 and March 2015, the unemployment rate for young Blacks was 29%, young Asians 24% and other ethnic groups 23%[79].

[79] House Of Commons Library (2015) 'Unemployment by Ethnic Background ', Accessed at: http://re-

This compares with a youth unemployment rate of 15% for whites at that time. Young people from ethnic groups are doubly disadvantaged in the labour market.

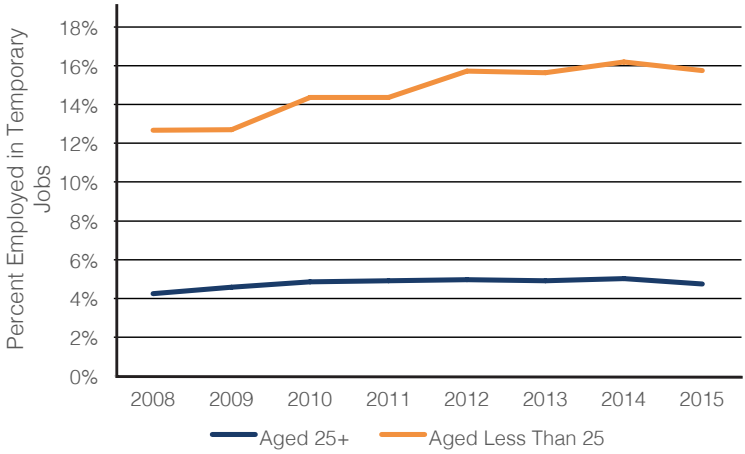
The overall youth unemployment rate also conceals the fact that many younger people would like to work more hours than they are currently being offered. We know this because the Labour Force Survey asks people how many extra hours they would be willing to work at the going wage rate. The young consistently respond that they would like to work more hours, while older workers typically prefer fewer hours. While the unemployment rate for the young has averaged 18.7% since the beginning of the Great Recession in 2008, the *underemployment* rate has averaged 26.2%. This statistic is calculated by adding the additional hours that individuals would like to work, converting these to worker-equivalents, adding these to the unemployed and calculating the "underemployment" rate using these additional worker equivalents[80]. It clearly confirms the idea that the young are being constrained to work fewer hours than they would like: as we shall see, this is likely to damage their long-term economic prospects.

The young are also disproportionately employed in low quality jobs. Figure 2 compares the proportion of those aged 25 and over that are employed in temporary jobs with those aged 16-24. The proportion of young people engaged in temporary jobs in 2008 was just above 12%. By 2015, that share was hovering around 16%. In contrast, there has been a much smaller increase in the proportion of older people working in temporary jobs. Employers are less likely to invest in training temporary employees: the consequence is again that opportunities to grow their productive potential are missed.

searchbriefings.parliament.uk/ResearchBriefing/Summary/SN06385#fullreport

[80] Bell, D. N., & Blanchflower, D. G. (2010a), 'UK unemployment in the great recession', National Institute Economic Review, 214, pp. R3-R25.

**Proportion of employees in temporary jobs by age**



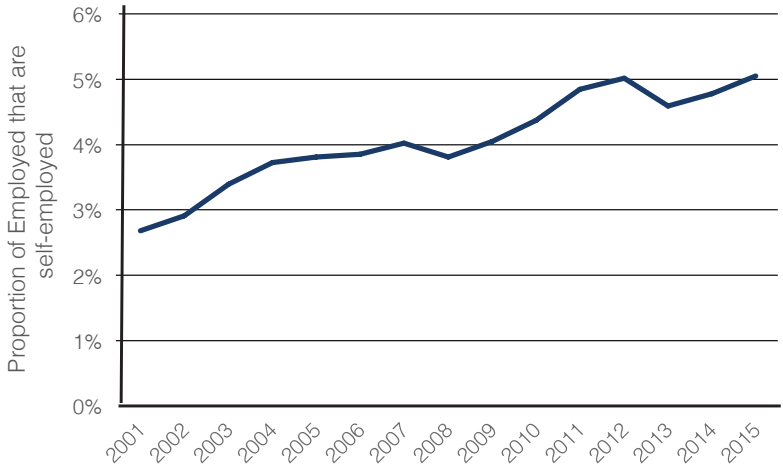

Source: Labour Force Survey

Another recent feature of the labour market for young people in the UK has been the dramatic rise in self-employment[81]. Self-employment is usually associated with older workers and indeed self-employment rates are much higher for older workers. But they have not been growing so fast as the young self-employed, whose numbers increased by 88% between 2001 and 2015. There has been a particularly rapid growth in the number of young graduates that are self-employed. This may be a result of a reduction in the number of large firms hiring significant numbers of graduates. However, it is estimated that the typical self-employed worker earns 40% less than the typical employee and that only 30% of the self-employed are contributing to a pension compared with 51% of employees[82]. The widespread belief that more self-employment, particularly among the young, is a panacea for the UK's poor productivity performance is clearly misplaced. Indeed, failure to accumulate adequate pension funds may mean this group becoming net beneficiaries of, rather than contributors to, the welfare state.

[81]Blanchflower, D.G. (2015), Self-employment across countries in the Great Recession of 2008-2014, Randstad.

[82] D' Arcy, C. and Gardner, L. (2014), 'Just the job-or a working compromise?' Resolution Foundation, May, Accessed at: http://www.resolutionfoundation.org/wp-content/uploads/2014/05/Just-the-job-or-a-working-compromise.pdf

**Proportion of young people in employment who are self-employed**




Source: Labour Force Survey

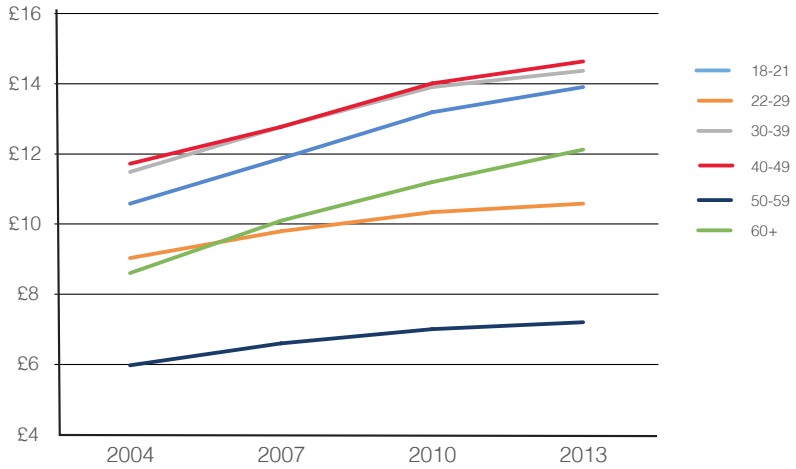
Self-employment is not a panacea for labour market problems. Clearly, the self-employed have more control over their working time and may choose to work longer hours than employees. Young self-employed workers typically work around 16% longer hours than their employed peers, but their hours are still less than those of employees aged over 25. Self-employment may be a way round the constraints on hours of work that many young employees face, but it is inherently riskier and generally less rewarding. This is particularly true for the young who are less likely to be able to access capital and whose returns will therefore be constrained to the value of their labour.

## 2. Youth wages

High levels of unemployment, underemployment, temporary job holding and self-employment do not provide a rosy picture of Britain's youth labour market. Each of these phenomena are likely to undermine productivity growth in this age group. This is already becoming evident from the wage data. Figure 4 shows hourly wages by age group for selected years from 2004 to 2013. It clearly demonstrates how hourly wages for those aged 18 to 21 have stagnated between £6 per and £7 per hour over this period. And while the earnings of those aged 22 to 29 have grown from £9.00 to £10.60 per hour, those aged over 60 have overtaken this group, with hourly earnings growing from £8.60 to £12.12. However, through market power or genuine productivity increases,

older workers outperformed the young during the period immediately prior to and including the Great Recession.

**Hourly wages by age group: 2004-2013**




Source: Annual Survey of Hours and Earnings

What are the consequences of bad outcomes in the labour market when young, such as those described above? There is strong evidence that such experiences when young have a long-lasting negative effect on young people's careers. Ingenious methods have been used to separate the effects of individuals' characteristics from the circumstances in which they find themselves. Gregg[83] related individuals' characteristics and information from the labour market in the locality when individuals were aged 16 to explain the number of months unemployment they experienced between ages 28 and 33. He suggested that the number of months of unemployment between the ages of 28 and 33 increases by two months for every three months spent unemployed *before* the age of 23.

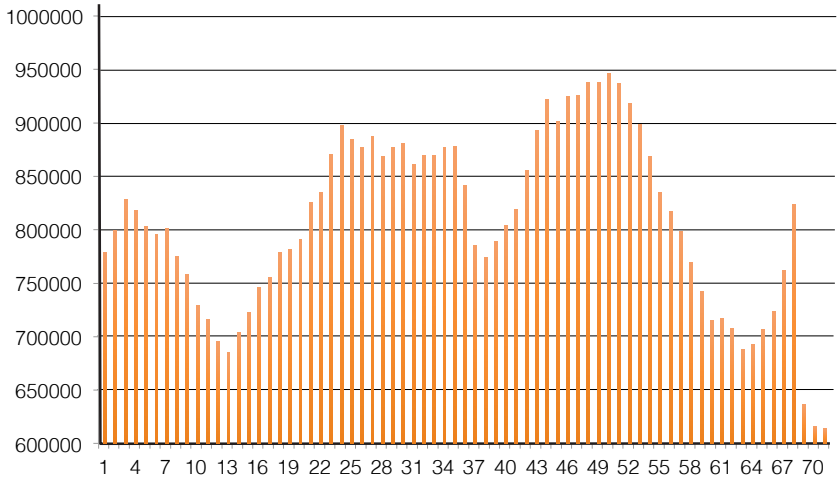
## 3. Demographics and rising youth unemployment

Figure 5 shows the UK population by single year of age up to the age of 70 using data from the ONS for 2014 which shows two spikes around ages fifty and thirty. Out of a total of 64.6 million, 7.8 million or 12.1% are age 70 and over.

[83] Gregg, P. (2001), 'The impact of youth unemployment on adult unemployment in the NCDS', The Economic Journal, 111: 626–653

In comparison 7.4 million or 11.5% are aged 16-24. Of interest also is that the size of the youth cohort was especially large when the Great Recession hit in 2008. For the age group 22-34 cohort size averaged 876,000, whereas those aged 35-40 only averaged 802,000. Cohort size for those aged 0-10 averaged 782,000 and for 11-21 average 762,000. The Great Recession hit in 2008 when there was a large youth cohort and falling demand so the young who were aged 16-24 in 2008 were hit by a double whammy - high labour supply and falling labour demand.

**UK population by single year of age in 2014**




## 4. Consequences of youth unemployment

Applying the same empirical strategy, Gregg and Tominey[84] find that there is a significant wage penalty of youth unemployment on males at age 41 such that their wages are 13-21% lower if they have repeated experience of unemployment when young. Evidence that those who choose to go to college or university are hurt if they enter the labour market during a recession is provided by Kahn[85]. She shows that the labour market consequences of graduating from college in

[84]Gregg, P, and Tominey. E. (2005), 'The wage scar from male youth unemployment.' *Labour Economics* 12.4, pp. 487-509.
[85] Kahn (2010), 'The long-term labor market consequences of graduating from college in a bad economy', Labour Economics, 17(2), April, 303–16.

a bad economy have large, negative and persistent effects on wages. Lifetime earnings are substantially lower than they would have been if the graduate had entered the labour market in good times. Our own research[86] is also consistent with scarring effects – either that spells of unemployment cause individuals to become disengaged from the labour market, or that unemployment acts as a negative signal to employers, making them wary of hiring.

## 5. Conclusion

What does this fairly depressing picture imply for the future of the welfare state? We clearly have a concern that the young have been particularly badly affected by the Great Recession. The concern is that many have been left behind and it would be a disaster if they were to become a lost generation. It is evident in their employment and unemployment patterns and in the slow growth of their wages. The difficulties have been particularly acute for young members of ethnic minorities.

There is a further concern that bad experiences when young impede transition to more productive activity: opportunity lost when young, becomes opportunity lost forever. Long spells of unemployment when young tend to cause permanent scars. Not only does this affect the individual's life experience, it weakens his or her ability to contribute to the welfare state. The old probably need to take heed as it is in their self-interests to engage the young. A major reorientation of policy towards youth employment, and skill enhancement seem essential but perhaps not sufficient to ensure the welfare state's longevity in its current form.

[86] Bell, D. N., and Blanchflower, D. G. (2010b), 'Youth unemployment in Europe and the United States', Nordic Economic Policy Review, number 1, pp. 11-38

# Alternative routes to full employment in a flexible labour market: Should welfare reform be tough, progressive, or radical?

John Philpott, the Jobs Economist and Former Director of Employment Policy Institute and Chief Economic Adviser at the CIPD

At the end of 2015 barely six years from the end of the worst recession in the post-War era, the UK working age employment rate reached a record high of 74.1%[87]. The unemployment rate meanwhile had fallen to 5.1%, below the pre-recession low. This is a remarkable achievement, vastly better than expected given the economic backdrop. The outcome is in part testimony to the success of a UK welfare-to-work model that has gradually evolved since the era of mass long-term joblessness in the 1980s and early 1990s. Yet despite its considerable success there is widespread acceptance that the current UK welfare-to-work model is in need of further reform, especially if judged against the objective of combining full employment in a flexible labour market with a marked reduction in dependency on means tested welfare benefits. Why is reform felt necessary? And how do alternative approaches to reform measure up?

## The current UK welfare to work model – success up to a point

Welfare-to-work policy isn't a form of government funded job creation but an umbrella term for a combination of supply-side measures that increase employment by improving the functioning of the labour market. The current UK model consists of two elements: 'make work pay', ensuring that people are always better off financially if they take a job rather than claim an out of work benefit and 'activation', requiring claimants to actively seek work as a condition of receiving benefit and if necessary to participate in programmes to help them into jobs. The various carrots and sticks contained within the model together serve to expand the supply of labour and dampen wage pressure. This enables the economy to run at faster pace of demand without breaching the rate of

[87] Office for National Statistics (2016) *Labour Market Statistics*, February.

price inflation targeted by the Bank of England which means more jobs and less joblessness.

The relative importance of incentives and activation within the welfare-to-work model remains a matter of debate, as does the cost-effectiveness of individual incentives and activation measures. But it's generally accepted that development of the model over several decades has helped boost employment to the current record rate, contributed to a halving in the structural unemployment rate from around 10% in the mid-1980s to around 5% today and reduced the proportion of the working age population who are economically inactive, which by the end of 2015 had fallen to 21.7%, the lowest rate for almost 25 years.

However, even at record employment, 29% of the 1.6 million people unemployed and seeking work have been without work for a year or more. In addition, 8 million people of working age are economically inactive, roughly a quarter of whom say they want to work. Not all these jobless people are on the welfare roll (in mid-2015 around 4.5 million were receiving an out of work benefit) and not all claimants are able to work because of illness, disability or caring responsibilities. Nonetheless, the still very high number of jobless people on benefit suggests the current welfare-to-work model can be considered successful only up to a point.

## Structural weaknesses in the current model

Receipt of welfare is primarily the consequence of economic and social factors plus personal misfortune that cause people to claim benefits rather than a reflection of some moral aversion to work on the part of claimants themselves. Indeed, given that by the standard of developed economies the UK places relatively few legal constraints on the terms of employment contracts and also has a relatively high proportion of low skilled people in the working age population, the success of the welfare-to-work model in moving people off benefits and into often very low paid or poor quality jobs is testimony to just how difficult it is nowadays is to scrounge.

Insofar as the ongoing welfare burden is attributable to the operation of the welfare to work model one can instead identify two essential operational weaknesses:

First, the carrots and sticks within the model have been applied most vigorously to claimants of Jobseeker's Allowance (JSA) and lone parent benefits and

generally proved easier to apply to people who are relatively young, able bodied and close to being job ready. The success of the current model is thus largely due to moving the more employable claimants of JSA and lone parents into work. This is particularly evident in the employment rate of lone parents with dependent children which rose by 8 percentage points to 64.4% between 2008 and 2015. The rate is now more than 20 percentage points higher than in the mid-1990s, the rise in part is responsible for a corresponding fall in the UK workless household rate from over 20% to less than 16%[88].

By contrast its proved much harder to help claimants of disability benefits, older people and very long-term welfare dependents whose attractiveness to employers is limited not only by prolonged joblessness but also often blighted by a history of homelessness, drug or alcohol abuse or a criminal record. For people in these categories, normal sticks and carrots are often inappropriate or need to be backed up by special return to work programmes. But tailoring programmes to meet the complex needs of different client groups is tricky especially if necessary investment is limited by tough public spending constraints. This explains why the welfare-to-work model has continually struggled to reduce the roll of working age claimants of incapacity related benefits. This stood at around 2.5 million in 2015 - little different from the total in the mid-1990s - leaving the employment rate for people of working age with a disability stubbornly below 50%.

Secondly, with the demand side of the UK's lightly regulated labour market fed on the supply side by an active welfare-to-work regime and a high rate of inward migration, employers face little difficulty in filling vacancies for minimum wage jobs and casual work. At present 1 in 5 employees are low paid on the conventional definition that their gross hourly earnings are less than two-thirds of the median wage[89] .

An abundance of poor quality jobs might reasonably be considered preferable to the structural unemployment suffered by people of low market productivity in more regulated economies with less active welfare to work regimes. But the obvious drawback of having a large number of working poor is strain on the making work pay element of the welfare-to-work model. In a marked change from a generation ago, nowadays fewer than half of people in the UK living

[88] Office for National Statistics (2015) *Working and Workless Households 2015*, October
[89] Corlett, A and Gardiner, L (2015) *Low Pay Britain 2015*. Resolution Foundation, October

below the conventional poverty line are in workless households[90]. This trend doesn't demolish the welfare policy mantra that 'work is the best route out of poverty' but it has weakened it. In order to incentivise work and alleviate in-work poverty, means tested in-work benefits are thus being paid to 4.5 million people, mostly with dependent children. Recipients range from people of limited means in full-time jobs with low average hourly earnings or in part-time jobs with low weekly earnings, to those in jobs with contracts that don't offer guaranteed hours.

In work benefits are necessary to help ease the work disincentive sometimes called the 'joblessness trap' caused by withdrawal of out-of-work benefits and the imposition of any tax people have to pay when they enter work. However, in-work benefits are themselves gradually withdrawn as recipients pay increases toward the level at which they exhaust their entitlement to support. This together with any extra tax liability recipients incur as they earn more imposes what for some can be a very hefty effective marginal tax rate on additional earnings, which can act as a disincentive to working longer hours and thus entrench underemployment. In addition, if employers have discretion over what they pay low productivity workers, knowledge of the withdrawal rate may influence individual pay bargaining with employees on in-work benefits and act as a drag on pay increases above the level of the statutory National Minimum/Living Wage.

## Reforming the model: the 'tough on welfare' approach

For all its headline success in fostering record employment, structural weaknesses in the current welfare-to-work model leave us with around 9 million working age people on some kind of benefit, split roughly equally between the jobless and the low paid. The policy challenge is to extend the welcome long-term decline in the number of people on out of work benefits – taking us closer to full employment - without simply offsetting this with a continued rise in the number of people in work reliant on the state to keep the wolf of poverty from the door.

The reform process underway since 2010 is geared toward full employment in a 'high wage, low tax, low welfare' country. However, policy continues to be heavily influenced by fiscal austerity as well as bearing the imprint of a 'tough on

[90] MacInnes, T, Tinson, A, Hughes, C, Barry Born, T and Aldridge, H (2015) *Monitoring Poverty and Social Inclusion 2015*. Joseph Rowntree Foundation and New Policy Institute.

welfare' ideology, which might undermine what will be achieved[91].

Ongoing changes to the make work pay element of the welfare-to-work model include: curbing the level of out-of-work benefits (exemplified by the Benefit Cap), the introduction of Universal Credit, increasing the amount people can earn before paying income tax, and raising the national minimum wage for people over 25 (rebadged as the National Living Wage) to 60% of median earnings by 2020. Running in tandem with these are changes to the activation element of the model that impose much tighter conditions on receipt of benefits, backed by tougher sanctions on people who fail to meet these conditions, and the operation of a single Work Programme (due to be superseded at some future date by a new Work and Health Programme) giving tailored support to help claimants into sustained jobs.

Many of these changes represent genuine potential improvements to the current model. For example, Universal Credit, a single simplified benefit which replaces six separate out of work and in-work benefits, each for a different client group and subject to distinct terms and conditions, is a welcome innovation. Universal Credit, notwithstanding the logistical (particularly IT) problems that continue to bedevil its introduction, makes it more worthwhile for claimants to enter work and/or work longer hours when in work than under the benefits system it replaces[92]. A significant innovation is in-work conditionality for most people receiving Universal Credit, who if working fewer than 35 hours at the statutory national minimum wage will be expected to look for more work or better paid work.

Also welcome is the differentiated payment-by-results system embodied within the Work Programme, which rewards programme providers only once they have managed to help a person into a sustainable job and offers higher payments for placing the harder to help[93]. This is in principle a sensible method of driving better outcomes albeit in practice the main achievement of the Work Programme has been to operate much more cost effectively than similar schemes rather than perform better at getting people into sustained jobs,

[91] Field, F and Forsey, A (2016) *Fixing Broken Britain? An audit of working age welfare reform since 2010.* Civitas, January.
[92] Brown, J, Hood, A and Joyce, R (2016) *The (changing) effects of Universal Credit*. Institute for Fiscal Studies, The IFS Green Budget, February.
[93] House of Commons Library (2015) *Work Programme: background and statistics*. Briefing Paper no. 6340, November.

especially older people, people with disabilities and the hardest to help[94]. In particular, the Work Programme doesn't seem to have avoided the perennial problem of all such programmes whereby providers 'cream' easier to help people leaving the rest 'parked' on benefit.

But whatever the overall merit of the ongoing reform process, fiscal austerity has resulted in a £5 billion cut in what was originally planned to be spent on Universal Credit, which will make the benefit less generous[95]. And instead of building on the cost effectiveness of the Work Programme by redirecting existing resources to help jobless people with disabilities, the new Work and Health Programme will be required to operate on a tighter budget.

More generally, the problem of viewing welfare reform through the prism of fiscal austerity is that policy success is measured not only in terms of getting more people into work but also by reference to savings made from cuts in the amount people can claim in benefit or how many are denied benefit. An obvious risk is that the tough road to full employment is one lined with far too many people living in hardship or reliant on food banks, which serves to devalue the purpose of welfare reform.

## Progressive evolution or a Basic Income?

The mainstream alternative to tough welfare reform is what might be described as progressive evolution of the current model. The aim would be to build upon useful policy innovations introduced since 2010 while at the very least maintaining benefit levels and investing considerably more in activation measures, with additional resources targeted at groups of clients with the lowest rates of job entry. This would represent a rebalancing of the model away from the orientation of recent years back toward the UK's 'tough love' welfare agenda of the late 1990s and 2000s. However, such a shift would at the political level require popular acceptance of the case for a high investment approach to welfare reform that might be difficult to gain in what has over time become a very anti-welfare popular culture.

Progressive evolution would also need to be buttressed by a coherent strategy to improve labour productivity, pay and job progression so that fewer people are reliant on in-work benefit. This might include a rethink on employment regulation

[94]National Audit Office (2014) *Department for Work and Pensions: The Work Programme*, July.
[95] Brown, J, Hood, A and Joyce, R (2016) *The (changing) effects of Universal Credit*. Institute for Fiscal Studies, The IFS Green Budget, February.

to reduce the possibility that employers subvert the spirit of the National Living Wage by expanding use of zero hours' contracts or self-employed contractors. It would, however, be naïve to think there is any silver bullet solution to the various challenges the flexible labour market presents to the welfare to work model[96]. The Holy Grail of higher productivity in the UK shows little sign of being found in the near future and without this there is always likely to be some negative trade-off between stronger employment regulation and jobs.

In this context, the case is often made to abandon evolutionary welfare reform in favour of revolutionary reform in the shape of Basic (or as sometimes known, Citizen's) Income[97]. This is an unconditional payment by the state to every citizen irrespective of means sufficient to provide a minimum accepted level of income. The entitlement is given by right regardless of whether or how much a person works, albeit earnings from work would be subject to a basic rate of income tax set high enough to finance the system along with everything else financed out of basic personal taxation.

Basic Income is unusual in being an idea that has advocates across the political spectrum. As well as reducing means testing, it eliminates the need for intrusive benefit conditions and sanctions and operates with the grain of a lightly regulated flexible labour market. There is no financial penalty or risk in taking a low paid or casual job, so it always pays to do some work, while the only disincentive to working longer hours is the marginal rate of income tax. Consequently, advocates reckon Basic Income helps promote full employment, though some see it is as a way of enabling people to remain financially secure and avoid poverty in a future world where advanced technologies might make jobs scarce.

Debate about the efficacy of Basic Income tends to revolve around affordability (with estimates that it would entail a basic rate of tax on earned income of at least 40%) and political saleability. But from a purely welfare-to-work perspective the key issue is that of conditionality. A well-funded Basic Income would in effect give everybody a no strings entitlement to a generous unconditional benefit. Although people might choose to top this up with earnings from work, UK experience tells us that even relatively ungenerous unconditional benefits more

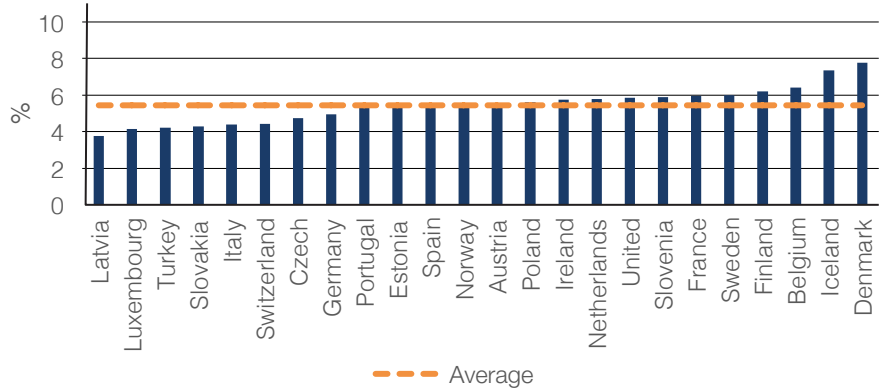
[96] Philpott, J (2014) *Rewarding work for low paid workers*. Joseph Rowntree Foundation, May
[97] Hirsch, D (2015) *Could a 'Citizen's Income' Work?* Joseph Rowntree Foundation programme paper, March.

often than not deter people from working. Basic Income thus looks like a very risky option if full employment is a policy objective.

This assessment might of course be different in a world of mass technological unemployment with far fewer jobs on offer but it is at present premature to recalibrate welfare-to-work reform on the basis of such a prospect. A generation ago when the UK's current welfare-to-work model was in its infancy there was also much populist talk of 'the end of work'. Yet even though since then the nature of work has changed considerably, posing fresh challenges to policy reformers, we have a greater number and proportion of our people in work than ever before. For the time being therefore we should continue to aspire to an evolutionary model that supports full employment in a flexible labour market without leaving millions of people mired in poverty.

# Education

## European expenditure on education (public and private) % of GDP, 2011

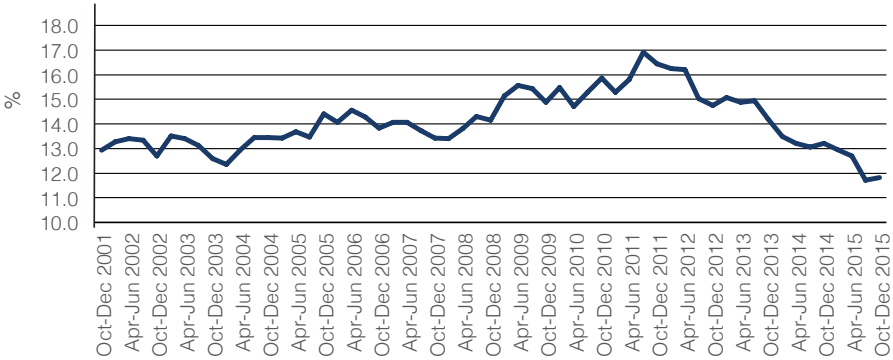



Source: Eurostat

**In 2011,** the **UK** spent **5.9% of GDP on education.**

**This is above** the **5.4% European average.**

## Percentage of 16-24 year olds not in employment, education or training

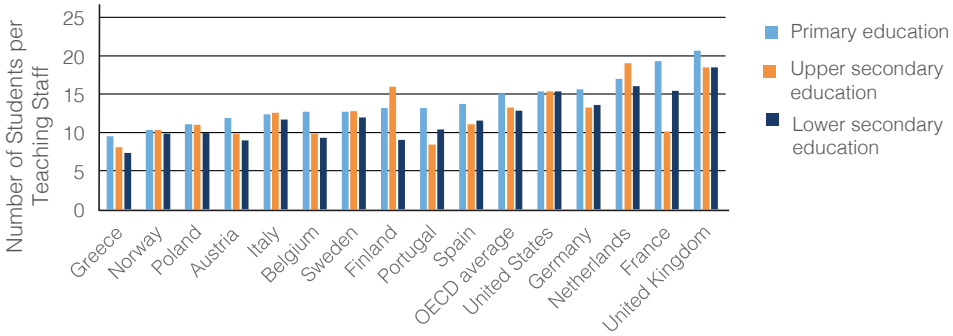



Source: ONS

**The number of "NEETS"** (Young people not in education, employment or training) has been **volatile over the years.**

**This percentage peaked in 2011** at **16.9% but fell to 11.8% by 2015.**

## Ratio of student to teaching staff 2013




Source: Eurostat

**The OECD average of students per teaching staff** is **15 in primary education and 13 in secondary education.**

**In the UK,** the **ratio is 21 pupils in primary education** and **19 in secondary education.**

# The individual and the social: making education matter for all of us

Professor Chris Husbands, Vice Chancellor Sheffield Hallam, Former Director of the Institute of Education, University of London

There has never been a time in the history of the world when education has meant more to more people than it does today. Around the world, individuals, governments and societies increasingly look to education as a vehicle for individual and social change: expectations of education are greater than ever. For policymakers and practitioners, education is **the** economic and social investment par excellence. In their analysis of American economic, technological and social development, "*The Race Between Education and Technology"* Claudia Goldin and Laurence Katz[98] argue that the twentieth century was the American century because American economic success was driven by education:

"Because the American people were the best educated in the world, they were in the best position to invent, be entrepreneurial, and produce goods and services using advanced technologies"[99].

The nation, they argue, that invested most in egalitarian educational opportunities and did that during the century in which education would critically matter was the nation with the highest per capita income. In the eighty years between 1900 and 1980, American education attainment improved rapidly and continuously. For the first three quarters of the twentieth century, they summarise, "education raced ahead of technology but later in the century, technology raced ahead of educational gains"[100]. The Goldin and Katz argument is enormously influential. In their 2015 education policy review, the OECD concluded that:

"…globalisation, innovation and growth have an important human capital

[98] Goldin, C and Katz, L., 2008, The Race Between Education and Technology (Harvard University Press)
[99] Goldin and Katz, p.2
[100] Goldin and Katz, p. 8

component, and the comparative advantage of many OECD countries has become their capacity to have highly skilled people [who] can work in knowledge-based professions"[101].

The evidence is overwhelming. Hanushek and Woessman[102] reviewed the evidence in 2010: the economic and non-economic returns to education are substantial. Across international datasets, the returns to individuals include a 13% improvement in salary to those who hold a degree, improved health – half the number of disabled years for those who hold a degree, longer life – an additional 1.7 years for every additional year of schooling. Higher levels of education are associated with lower offending, higher levels of physical activity and improved social cohesion[103].

But if education is the key driver for social improvement, it can also be highly regressive. It is a positional as well as a social good. It preserves the power and authority of the already privileged. In 2014, 0.1% of year 11 pupils who claimed free school meals and who took A levels or level 3 qualifications went to Oxford or Cambridge.[104] Conversely, the Sutton Trust found in 2011 that four highly selective independent schools - Eton, Westminster, St Paul's Boys and St Paul's Girls - and state-funded but highly selective Hills Road Sixth Form College in Cambridge, between them sent almost a thousand pupils to Oxford and Cambridge between 2007 and 2009 – more than the 2,000 least successful schools in this respect[105]. Investments in education across social classes have diverged. Greg Duncan and Dick Murnane pin down the American data. In 1973, the richest quintile of American families spent $2,700 more on child enrichment activities than the poorest quintile. At constant prices, by 2006, the figure had tripled to $7,500[106].

This is the paradox of education in the twenty-first century. Education is seen as the magic bullet; the first call on investment; the intellectual infrastructure. It

[101] OECD, 2015, Education Policy Outlook: making reforms happen, p. 22
[102] Hanushek, E., and Woessman, R., (2012) "Do better schools lead to more growth" Journal of Economic Growth
[103] OECD, 2012
[104] Grove, J. "Oxbridge Access: DfE releases free school meal stats", Times Higher Education, March 21, 2014
[105] The Sutton Trust (2008) University Admissions by Individual Schools. For a response from the University of Cambridge admissions director, see http://www.admin.cam.ac.uk/offices/admissions/behindtheheadlines/admissionsschools.html
[106] Murnane, R., and Duncan, G., 2012, Whither Opportunity: rising inequality, schools and children's life chances Ruseel Sage Foundation), p. 11

will make societies more productive, healthier and safer. It will equip children with what they need in a world in which the returns are to the high skilled. It will enable our children to produce the wealth which will look after us as we age. And so on. But it's a treacherous friend. It reinforces inequalities and embeds divisions.

For the past thirty-five years, education policy in England – and across the Anglophone world – has emphasised the positional rather than social purposes of education. Policies such as extending parental choice (the 1981 Education Act), devolving budgetary management to individual schools (the 1986 Education Act), the introduction of regular, published inspections of publicly funded schools (the 1991 Education Act), the introduction of new types of school and school providers (the 2002 Education Act), and the extension of academisation across the entire school system (the 2016 Education Bill) the introduction of 'free schools' (the 2010 Education Act) and the extension of academisation across the entire school system (the 2016 Education Bill) have had the combined effect of focusing the purposes and functions of Publicly-funded education around the individual attainment and life trajectory of individual learners. This has been a focus of policy under Conservative, Labour and Coalition governments: it is not party political. The consequence is a school system which is focused on, and held accountable for its success in securing individual positioning for learners. One specific development summarises it: as from 2012, the secondary school performance tables included a 'destination' component noting how successful each school was in securing entry for its alumni to the most selective, self-identified 'elite' 'Russell Group' universities.

There's no doubt that this sweep of policy has secured some positive results. Standards of performance, measured by examination results, are higher than they were. In 1959 – the year I was born – just 9% of young people secured the equivalent of 5 or more A*-C GCSEs; more than 9 out of 10 children left schooling with no qualification to show for their education. In 2015, over 50% of sixteen year olds secured the equivalent of 5 or more GCSEs at A*-C. Those who long for a 'traditional' education forget that in too many cases, it simply failed large numbers of young people. At the same time, the standard of schooling has risen. Intensive school inspection and an increased focus on teacher performance have to all intents and purposes driven systemic school failure out of the system. These are exceptional achievements, and the fact that

they are not routinely celebrated more often is simply a reminder that we now take them for granted. We expect young people to go to successful schools and to achieve.

But it's an iron rule of public policy that all gains also involve losses, and the sheer strength of the focus on education as a positional good has meant that we have lost sight of some of the other functions of education: its purpose as a social good, promoting collective as well as individual ends. Particularly in urban areas, the hierarchy of schooling types has become dizzyingly steep. Despite the real improvements in performance, the school system remains as selective in its performance as ever, as that statistic about entry to Oxford and Cambridge suggests. Publicly funded education is not simply a positional good, not simply a vehicle for individual social mobility[107], but a social good. It is and remains a tool by which we socialise the next generation, preparing them not simply for access to a selective university and careers, but for active citizenship and participation in adult society. The 1988 Education Act, which introduced the national curriculum, in a rather curious clause, captured this. It provided that 'the curriculum for a maintained school (must be) a balanced and broadly based curriculum which (a) promotes the spiritual, moral, cultural, mental and physical development of pupils at the school **and of society**; and (b) prepares such pupils for the opportunities, responsibilities and experiences of adult life.'[108]: the curriculum should concern itself not simply with pupils' academic attainment ('mental…development') but also with their spiritual, moral, cultural…and physical development', and it should be concerned not just with 'pupils at the school', but also – the curious phrasing – with the development of 'society'.

Much has changed in English education and society since the passing of the 1988 Act, but the Act remains in statute, and this concern with the wider purposes of schooling remains relevant. Indeed, in a society which is more economically unequal in 2016 than it was in 1988, which is more culturally diverse in 2016 than it was in 1988 and which faces tougher choices about the allocation of public funds in 2016 than it did in 1988, it's no bad thing to think again about what that clause means for education and its place in public policy.

[107] Social Mobility and Child Poverty Commission (2015) "State of the Nation 2015: Social Mobility and Child Poverty in Great Britain"
[108] Education Reform Act 1988 (c. 40). Part I, Chapter I, Section I (2)

## Reforming education

One of the most fundamental – indeed, irreversible – changes has been the extension of academy status across the English school system. What this means in practice is that schools have passed from the management of local authorities to the management of boards of trustees who direct either individual or, increasingly, clusters and chains of schools. Local authority assets – the land and buildings in which the school is based – have passed from public control to the control of boards of trustees. In the 2015 Autumn Statement[109], the Chancellor actively looked to a future in which local authorities played no part in education. All schools would be independent entities. This would be the logical extension of the policy trend which began with the 1981 and 1986 education acts: every school an independent school; every school a tool for positional advancement. But the revenue and capital funding base for education remains publicly funded. It follows, I think, that the spirit of the 1988 clause requires that those receiving public money for the provision of education to those up to the age of 18 recognise their commitment to a number of core principles. First, the explicit acknowledgement that education is a public as well as a personal good and that it serves the common good as well as individual attainment. Second, those in receipt of public funds should be required formally to acknowledge that schooling is one of the means by which we both realise individual potential and build a socially just and cohesive society. A consequence of this is that behaviours which advantage the learners who happen to be at one school rather than another should be regarded an unacceptable, whether that is 'poaching' teachers or excluding the hard to educate. Third, those in receipt of public funding recognise that individual schools are part of a commonwealth of schools and other agencies which work together to contribute to the education and development of the young people in each community, and should be obliged, by virtue of their receipt of public funding to collaborate with one another and with other agencies to secure outcomes which benefit all.

Several things follow from these principles. It follows that all those providing public education will necessarily be subject to current legislation in relation to good practice in corporate governance, employment law, diversity and equality laws, health and safety and other related laws. This does not prevent schools from adherence to specific religious or other traditions, but it does mean that they should be formally required to respect legal and ethical frameworks which

[109] https://www.gov.uk/government/topical-events/autumn-statement-and-spending-review-2015

relate to the common good. It means that those providing public education should comply with the same framework as all other maintained schools in relation to the educational legislation and guidance on for example, admissions, exclusions, curriculum, inspections, and so on. At a time when the diversity of school types is increasing rapidly, it would be politic to require the providers of education to agree to a Nolan test (or equivalent) for Trustees ensuring that the processes by which they are appointed is open, transparent and fair and that those appointed as Trustees and Governors are aware of their obligations in respect of education as set above, and that they should ensure that the local community is appropriately represented on the body of Trustees. They should be required to implement corporate governance requirements relating to conflicts of interest in the supply of goods and services and desist from using their school to promote particular views. They should be required to collaborate with other local schools to implement educational policies that require shared actions, such as the education of 'hard to place' pupils, extended services and community and arts development.

We live in an increasingly unequal world: the share of wealth owned by the wealthiest 1% is higher now than at any point in the last century. It is not surprising that in an unequal world, parents should seek to ensure that education benefits their own children and positions them as strongly as possible for success. But education remains a public good. It is our message to the next generation. We should not, ever, deny parents their aspirations for their own children, but we should remember that there is a social as well as an individual interest in education. It matters to all of us and we should ensure that those who shape it reflect the shared interest we all have.

# Education in the twenty-first century

Anthony Seldon, Vice-Chancellor of the University of Buckingham

The year is 2016. Yet, incredibly, Britain has not developed a twenty-first century education system, nor one that even fully adapted itself to the demands of the twentieth century, but one which remains, in most vital respects, nineteenth century.

Children go to school in nursery and primary schools up to age eleven, or Year Six. Primary schools are typically for between 200 and 500 children, and class sizes are on average about thirty. After they leave, they go on to secondary school until their GCSE exams at the age of sixteen, after which some will leave and others stay on to sit A-Levels at age eighteen at the end of Year Thirteen.

Some forty percent of young people move on to higher education at university, typically between the ages of eighteen and twenty-one, where they will sit three year degrees, after which the great majority will leave with a second class degree. Their education is now officially at an end. Other young people will go on to technical or vocational pathways to complete their education. Once their training is completed, their formal education, too, comes to an end.

This system, which can be called the "factory model" of education, is substantially de-personalised. The entire process is akin to an industrial production line, with young people joining it at the age of three or four. A series of "injections" of information are then inserted into the individual until they leave the process at the age of sixteen/seventeen/eighteen/twenty-one, or later, often with a certificate to verify that the process has taken place. A small percentage of school students attend private schools, where they have up to five times as much money spent on them, as those in state schools. Those who come from the most moneyed backgrounds, with the most social capital at home, and the best connections, thus enjoy the best funded schooling. Unsurprisingly, the students depart from these schools to the top universities and top jobs.

Uniformity of progress is a core characteristic of this industrial model. It is

narrowly academic, with little interest taken in non-academic pursuits. It is exam based, with students sitting at desks in long rows overseen by invigilators, answering question-papers on their own, which require them to perform actions recorded on paper or on screen, requiring memory and the application of learnt skills. The learning throughout the years at school and university is often passive. The teacher or lecturer stands at the front of the class or lecture hall giving out information about a subject. The students then carry out instructions, either on their own or in groups.

Schools and universities are physical spaces to which students travel, usually for the working day. In some "boarding" schools—mainly but not exclusively in the independent sector—students remain at the institution during the weeks of term, as is the case for many at university. There is little interest in the development of the whole student, including their artistic, creative, sporting, moral, and personal dimensions. Their wellbeing is principally of interest only in as far as it can enhance their performance. The whole process focuses on assessment of work by the individual, with assessment only of their academic performance in exams and practical assessments. It is assumed that the students will be taught knowledge which is objective fact, the truth of which will remain unchanged and be largely unchallenged. Students excel if they produce the "right" answers in the "right" way.

But we live in the 2010s, not in the 1850s, or even the 1980s. We need to move to a twenty-first century education model, one which will be radically different.

**1. *Digitalisation***: Within the next ten years, advances in artificial intelligence and computing will mean that the holy grail of personalised learning will become a reality for all, and at prices which schools and universities can afford. Smart A.I. machines will adapt academic subject material to the particular learning styles and learning difficulties of each individual student, and will quickly develop a whole diagnostic understanding of each individual student and their educational profiles and learning needs. Much more learning will take place online, with students able to move at their own pace, and with a computer adapting the material to be studied in a way that is individually tailored for each student. The learning will have much more in common with the stimuli used in computer games to attract the interest of the student, and to make them actively involved in learning and discovering. The pace of learning will be considerably differentiated and accelerated. The process will become much

more enjoyable for each individual student as they can now proceed at their own natural rate of progress rather than having to fit in with the aggregate needs of the class. Lessons will still offer ample time for teacher exposition and group work by students, but much more time will be given over to individual study in front of screens. Homework will similarly be much more computer based. Education will become "flipped", with students learning and discovering on their own, and lessons being used for discussion, clarification and deepening of understanding.

***2. Stage not age:*** At present, for a significant proportion of each age group, the rate of progress is either too slow or, for another significant proportion, it is too fast. Those who are moving at the former pace become bored and can become resentful and disruptive, while those for whom the pace is too quick can become alienated and detached from learning. Digital learning will mean that students no longer have to move at the aggregate pace of the class as a whole, but can move at their own individual pace, which would vary between subjects. A student might find that they can move at a much quicker rate when studying foreign languages or science than they can when studying history or English. Schools will still be organised on the basis of year groups—not least because this is important for social development and self-esteem. But within each year group there can be a considerable range of pace at which each student is moving, and hence a considerable range in the rate at which they will be ready to pass through new exam thresholds.

***3. Exams:*** The whole pattern of every student sitting key exams at certain stages of their lives, involving the hit-or-miss of how they feel on the day, and the inevitably subjective element of how exams are marked, will be ended forever. The computer programmes monitoring each student will be able to give a real-time performance record of each student's ability in every subject. The computer programmes will generate an entire learner profile for the student, citing their particular strengths and aptitudes as well as their weaknesses and areas for development. At present, exams take a considerable bite out of each academic year, yet arguably are not a good preparation for life. Nothing that anyone will encounter in life equates with the exam process of sitting in long rows for two or three hours and writing answers alone. Some students are "good" at exams, while others are poor, but this difference can bear little correlation to their aptitude at each subject. Universities, employers, schools,

and the students themselves, will in future have considerably more information about their abilities, aptitudes and interests. Students who are making quick progress at school will begin university modules whilst still there, and gain credits before they even arrive at university.

***4. The three-year university undergraduate degree residential model:*** We are now in the last few years of the model where undergraduates go *en masse* to universities where they live for three or perhaps four years, before gaining an undergraduate degree. Typically, the workload is comparatively light in the humanities and social sciences, while considerably more intense in STEM subjects. Digitalisation means that students no longer need to work in university libraries because the material is much more speedily available online. It means that they no longer have to attend university lectures because they can listen to lectures given by the university academics on their intranets, and to lectures by academics elsewhere in the world, which are readily available online. It means that they no longer need to travel to seminar rooms to take part in discussion, which can now take place online. The time at university can be shortened, as at my own institution—the University of Buckingham—where the standard degree takes only two years. Rather than spreading the work over three years, with very long holidays—particularly in the summer—Buckingham has four terms a year, and works for forty weeks. Thus, three years' work can be packed into just two years. Some undergraduate degrees in future may be sat in less than two years, while others will be spread out over four or five, and still others taken online.

***5. Lifelong learning:*** The idea that we leave school at eighteen, or further education and university aged twenty-one or twenty-two, and education for life is then over, has to be profoundly rethought. The twenty-first century will be one of continuous education—for work as well as for life. The constantly changing demands of the workplace will ensure that we need to reconceptualise our understanding of education. The idea that we can train lawyers, medics, accountants, teachers, managers, and the rest, for life at a young age, and that these skills will be embedded for life, is palpably absurd. Siemens is one of many companies which used to have a radical rethink of the way that it operated every ten years. That subsequently came down to five years. Now it is finding that it needs to rethink its entire *modus operandi* every year, or even more frequently, according to Juergen Maier, CEO of Siemens in the UK. Equally, because

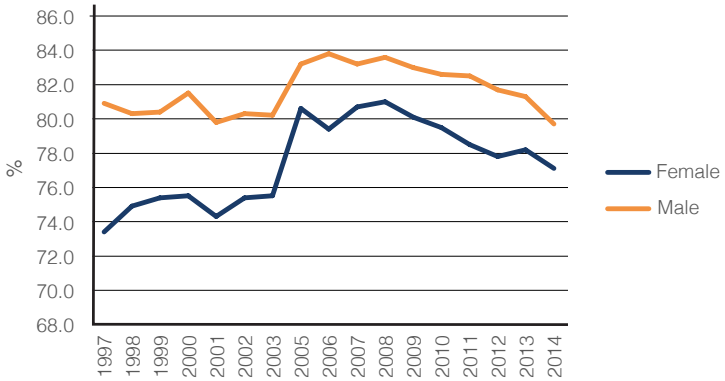
there will be more leisure time in the twenty-first century—compared to the nineteenth century when factory workers worked far longer hours—we need to embrace far more fully the notion of lifelong learning for pleasure and enjoyment of life in all its forms. Courses and programmes, whether for degrees, diplomas, or without formal qualifications, will proliferate, as will subjects such as history of art and architecture, literature, foreign languages, astronomy, and biological sciences. The twenty-first century will be an age that will see an upsurge of curiosity and wonder at all aspects of the universe, from the furthest stars to the smallest subatomic items of matter.

**6. *Wellbeing:*** The nineteenth century and twentieth century education models gave little space for the development of the quality of human life. They were obsessed with outward metrics of exam passes, tests, and other quantitative measures. The early twenty-first century saw a flowering of interest in wellbeing and "positive psychology", grounded on the thinking that young people can develop habits of mind and practices from an early age that will allow them to negotiate and to navigate their way more successfully through life. Thinking skills are core in this; these include the building up of resilience and grit within young people, the ability to cope in the face of adversity, and to relate successfully to other individuals and to groups. Physical health, too, lies at the core of this approach. Young people in future will be taught to understand better how their own bodies work, and how to breathe and stand well, what to eat and drink, how and when to rest, sleep, and relax. Even middle aged and senior citizens will learn much more about their wellbeing, and about how to lead more autonomous, happy and successful lives.

***7. Enhanced opportunities for all:*** The factory model of education never managed to enhance social mobility in Britain. Britain in the early twenty-first century, in significant ways, remains as hierarchical as it did in the twentieth and nineteenth centuries. Digitalisation and the new learning methods described here will achieve in future what the best minds in the country never managed in the past. The ubiquity and cheapness of this new learning technology will ensure that able minds from all social classes will be stimulated, and will have a much better opportunity to show their merit and capability. It will take many decades before Britain becomes a fairer society, where the able from whatever social or ethnic background will have the chance to fulfil their potential. But we are at last on the road.

***8. Back to the Future:*** Education in the twenty-first century will be based on the medieval idea of the "trivium", grounded on grammar, logic, and rhetoric; grammar to express thought, logic to organise it, and rhetoric to communicate it. Following the trivium, students traditionally progressed to the quadrivium, which originally consisted of arithmetic, geometry, music, and astronomy. These constituted the seven liberal arts of classical antiquity, and were later expanded to include subjects such as history and moral philosophy. Even though human knowledge will grow, the need for a broad education on the lines of the liberal arts model will remain, to enhance interdisciplinary thinking, flexibility, and creativity. Everything may appear different in the twenty-first century, but the fundamentals of human existence will remain, even—especially perhaps—for those studying science and technology.

## % of total life spent healthy, UK (2014)

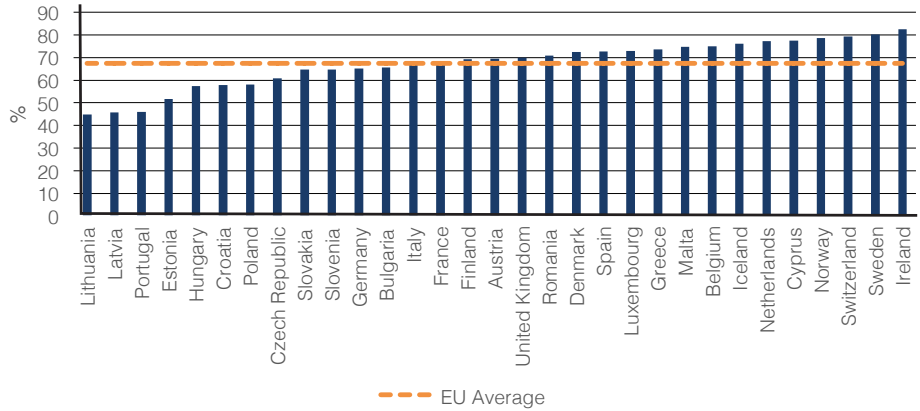



Source: Eurostat

**In 2014, men** are likely to spend **79.7% of their total lives in good health.**

**Women** are likely to spend **77.1% of their total lives in good health.**

## Proportion of people in subjective good health, (2014)

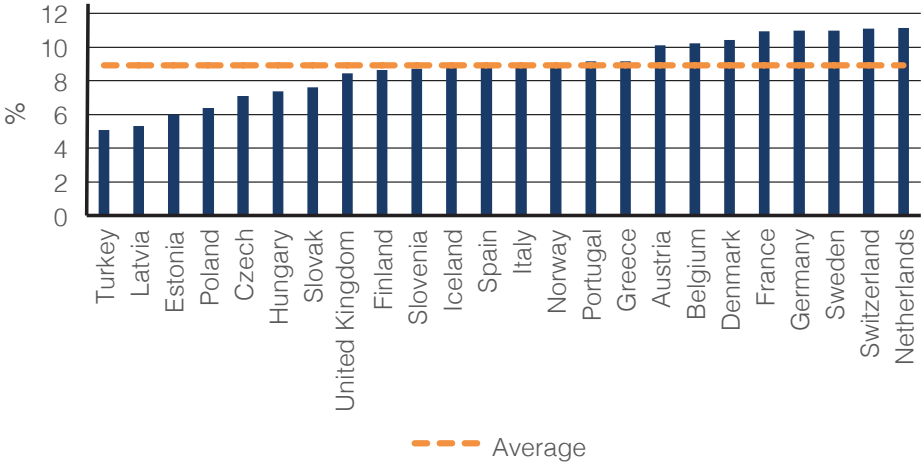



Source: Eurostat – Data aggregated from very good/good, fair and bad/very bad

**On average**, **67.4% of EU citizens** describe themselves as either in **good or very good health.**

**The UK** performs slightly better than the **EU average with 70%** of the population describing itself in **good or very good health.**

## Total european healthcare expenditure as % of GDP, 2013




Source: Eurostat

**In 2013,** the expenditure on **healthcare as a proportion of GDP in the UK was 8.5%, below the European average of 8.9%.**

# Rethinking health care and taxing assets to fund social care

Phil Hope, Former Minister of State for Care Services, Director of Hope Consultancy, and Visiting Professor at Imperial College

## Introduction

The demographic challenge we face is clear[110]. We are living longer which is a cause for great celebration but unless we live well for longer, the increasing demands from an ageing population will mean the health and social care system will not be able to cope. Current proposals for NHS reform are good, and recent developments in social care funding and devolution may offer new opportunities. But these changes are insufficient when the NHS continues to run an annual budget deficit and nearly two million people over the age of 50 have unmet care needs[111]. Our health and care policymakers are stuck in old ways of thinking – a clinical view of the world, operating in silos, with insufficient and inefficiently distributed resources.

## What needs to be done?

It is the sum total of the statutory, voluntary and private sector services alongside all the informal networks of family, neighbours, friends and community groups that actually make up our health and care system. And it is the efforts we make to look after ourselves and the policies to help prevent our future ill-health that ensures we all have healthier and happier lives as we get older. Marshalling and enabling all of that resource is the only sustainable approach to meeting the challenges of an ageing population.

Yet during my seven years as a government Minister I found that approach very difficult to apply in practice. I was always responsible for one silo or another - local government, skills, the third sector, carers, mental health or care services – and then only for a relatively short term horizon of 2-3 years at best. In that

[110]Britain's greying population, RGS, 2015
[111]The end of formal social care: a provocation, ILC UK, December 2015

regard, the NHS Five Year Forward View[112] is a necessary and substantial shift in approach to thinking more broadly about people's health and services. But it is not sufficient.

The strategy is still rooted in an essentially clinical view of the world with change directed by NHS leaders, and primarily aimed at reform of and within NHS structures, services and procedures. Where, for instance, is the Social Care Five Year Forward View? A reference to local examples of best practice in joint working is not enough. Too many hospital beds across the country are occupied by older people medically fit for discharge but unable to go home because of insufficient social care services. Flat-real budgets for the NHS at the same time as major cuts in social care budgets is silo-thinking nationally that is undermining NHS reform locally.

Integrating health and social care alone is not enough either. Given what we know about the 'non-clinical' drivers of high clinical cost of older people such as loneliness, unsafe homes, or ineffective self-care, where is the comprehensive strategy to address these issues?

Where too, is the active promotion of charged-for help-at-home services that older people pay for from their Attendance Allowance, Personal Budgets, or from their own or families' private income? And what about a substantial increase in the personal and financial support for informal carers without which the system would collapse and whose contribution is identified in the health strategy but whose needs are rarely recognised in practice. Very often it is third sector organisations at the forefront in addressing all of these wider elements, yet where is the serious long-term strategy for ensuring their growth and engagement as part of a sustainable system?

## The key elements for a sustainable system

The key elements of a strategy for creating sustainable health and care services in ageing societies were outlined in the report[113] of a working group I chaired for the 2012 Global Health Policy Summit. The group identified care innovations from around the world in four main areas - getting the financial system right, helping families to care, implementing prevention and self-management programmes that reduce demand for care, and improving value for money in

[112]The NHS Five Year Forward View, NHS England 2013

[113] Hope, P. et al (2012) "Creating Sustainable Health and Care Systems in Ageing Societies" Report of the Ageing Societies Working Group 2012

the supply of care.

Most of the work currently underway in England is however focused on just the last of these. Simply finding and implementing efficiencies across the system to reduce waste through better procurement of goods and services, back-office savings and reducing the use of expensive agency nurses will not deliver the scale of savings required. The QIPP programme, the Better Care Fund schemes, the Vanguard and Integrated Personalised Commissioning sites and other local initiatives need to be judged against more rigorous and radical criteria of success.

Do such programmes just patch up the current system or should there be more radical change interventions that turn over the 'care triangle' to achieve better health outcomes and move spending from expensive institutional care (hospitals and care homes) to lower cost care at home?

Can they be better targeted for more immediate gains by identifying people at risk of high health costs and then acting to prevent their unplanned admissions or re-admissions into hospital? This is particularly important for older people with dementia for whom hospital is the last place they need or want to be, and whose comparable length of stay and cost is much longer than it should be.

Do these programmes have, as a central goal, that people should receive the right care in the right place at the right time at the lowest cost by re-aligning the financial incentives across the system?

Are health and care commissioners working in partnership with new third sector and private providers to deliver services along whole care pathways, not just parts of those pathways, with a cap on profits or national benchmarks for their return on capital[114] to ensure a good deal for the taxpayer?

And is every innovation a frugal innovation that is assessed to ensure its cost is less than the old service or product it seeks to replace?

## Beyond clinical solutions

The biggest concern however is that most of the change programmes now underway still appear to be rooted in a clinically-driven analysis of the needs of an ageing population. Inevitably this leads in turn to clinically-based solutions to meet those needs, which can be as expensive as the institutional care costs

[114]Laing, W. (2015) "Stabilising the Care Home Sector and Preparing for Implementation of Part 2 of the Care Act in 2020" A white paper, LaingBuisson

they seek to reduce. This is cost substitution not cost reduction and just as unsustainable.

The reason for many older people's high level of unplanned admissions, readmissions, frequent visits to the GP, and increasing demand for community health services and social care packages, is not poor clinical care. Rather, it is rooted in other aspects of their lives that lead them to demand more of the care system. The stories of older people's lives in Age UK-led integrated care programmes[115] reveal the drivers of high clinical costs as often being about older people feeling lonely, not having any purpose in life, being socially isolated, feeling unconnected to community, being mildly depressed, feeling unvalued, lacking resilience, not managing their condition or medication well, being physically inactive, living in a damp, cold or unsafe home, and not coping with living on a low income.

These new programmes focus on achieving personalised quality of life goals which address the non-medical aspects of their circumstances and which shift people from a position of high dependency on the system to that of greater independence and control of their own lives. The cost is actively managed to be less than the amount saved elsewhere in the system from reducing people's demand for statutory services.

The biggest challenge to making these programmes succeed has been persuading the clinicians and the social workers to actively recognise that this approach - not more clinical care - is what works. A critical element is the development of multi-disciplinary teams including the third sector that deliver the best quality clinical care, social care and community support.

## Prevention

Shifting from being a 'sickness service' to a 'health service' with more action 'upstream' to reduce the drivers of ill health is also key to tackling the longer-term pressures. Our report in 2013[116] on applying evidenced-based best practice methods for reducing the risk factors associated with developing dementia such as diabetes and hypertension, showed the potentially huge benefit in reduced costs and reduced years of life lost in a new dementia prevention strategy.

[115] Age UK Personalised Integrated Care Programme, Age UK, 2016

[116] The International Longevity Centre, (2014) "Preventing Dementia: a provocation. How can we do more to prevent dementia, save lives and reduced avoidable costs?"

Screening for the over 40s to identify people with these risk factors in order to use proven interventions with those where the risk and cost benefit is greatest is a big step forward. The public health challenge now is to identify interventions that are shown to have a sustainable impact on shifting people's lifestyles including taking more exercise and reducing mid-life obesity, and then driving these interventions forward.

'Light touch', low cost interventions with larger numbers of older people at risk but not yet causing high cost are also important. Straightforward low-cost information and advice on preventing ill health, avoiding accidents at home, staying physically active and maximising income to spend on help at home or community activities to keep well must be part of a wider prevention strategy.

The more difficult political challenge of reducing the presence of known causes of ill-health such as high levels of sugar, salt and fat in our food will have to be addressed. The Treasury argued that compressing morbidity (ensuring people living well for longer) is the real long-term answer to the cost time-bomb of an ageing population and the new sugar tax is a landmark step forward. But a sustained public campaign for change is required to create the climate in which Ministers have the confidence to go further, faster. Banning smoking in public places felt a tough decision at the time but became the norm almost overnight.

**New sources of funding beyond income tax**

Putting more resources into the current configuration and thinking about services would simply maintain a financially failing model for a short while longer. And more resources will still be required in a reformed system to meet the inevitable growing demand from ageing.

Relying on income tax alone to pay for the cost of ageing is not an option as the extra burden of taxation on the working population would almost certainly be financially unsustainable given the changing dependency ratio. Despite extending the State Pension Age in the future, tax revenue from a shrinking working age population will not be enough to fund the health and care services required by a growing and ageing population.

Private funding solutions alone will not suffice either. Private equity release products exist but many older people are reluctant to use their housing assets to fund their care costs[117] so will these products develop at sufficient pace and

[117] Equity Release Council (2012) "Making the most of Equity Release", edited by Lord German

scale to solve the fundamental challenge? Insurance products for people to cover themselves against future care costs may not be affordable to most and, similarly, may not operate at sufficient scale to cover the potential liabilities of very high care costs for certain groups such as those who develop dementia. Even if the Dilnot proposals for a cap on care costs to limit these financial risks are implemented, it is uncertain whether the insurance industry will respond in the way that the government hoped, while care providers have raised serious concerns about the impact of the care cap on the private care market[118]. The care cap has now been delayed for at least 5 years, if not indefinitely, so for now, at least, this does not appear to hold the answer.

Instead, the government have turned to taxing property to generate new income. Local Authorities responsible for social care services can now introduce a local care levy of a 2% increase in their council tax, the proceeds of which must be ring-fenced for spending only on care services. It is a policy that has echoes of the national care levy - a hypothecated tax on property after people have died - that we explored as a means of funding a comprehensive national care service but with a local twist. Council taxes are property taxes, and, despite deep Treasury opposition to this at a national level, the sum raised locally is also hypothecated or ring-fenced.

Unfortunately, this new property-based tax for funding social care has a number of major disadvantages compared to a national care levy. First, Government estimates[119] that the total amount it raises each year will be £2bn by 2019/20 billion but some commentators suggest the actual value is nearer £800m[120] which is simply not enough to cover cuts elsewhere let alone respond to growth in demand and may end up being used to pay for the unfunded increase in the national minimum wage. Second, council tax is also quite regressive in its impact on local tax payers with the poorest paying disproportionately more, so may not be viewed as fair taxation to fund social care for an ageing population. Third,the distribution of the income it raises varies massively between councils in different economic areas with the areas of most need raising the least income[121].

Intriguingly however, now that taxing property to fund social care is a reality,

[118] Stabilising the care home sector, LangBuisson, 2015
[119] Spending review 2015, HMT, 2015
120 King's Fund analysis, The Guardian, 6th December 2015
[121]The International Longevity Centre (2015) The End of Formal Adult Social Care

this may be a good time to re-open the broader idea of tapping unearned income from rising house values. This wealth has not been earned by 'thrifty hard working families' but is a bonus accruing to a lucky segment of the older population who are thus both a primary cause of the financial pressures on the health and care system, and fortuitous owners of a growing resource that could be taxed fairly to meet those costs. The lottery of what amounts to a 'dementia tax' on those who have to sell their homes to pay for long periods of unfunded care would be replaced by a shared care premium on all property (a flat-rate or a percentage) to meet the care needs of everyone. And we could still meet people's understandable ambition to pass on the bulk of their wealth to their children or grandchildren.

A second major area of funding reform is the proposal to move Attendance Allowance worth around £6bn from the uncapped DWP (AME) budget to the capped DCLG (DEL) local government budget. The debate has only just begun but it is difficult to see how local authorities will be able to fund non-means tested, needs-assessed payments to older people to spend on services of their choice if the budget they receive is capped. Demand could quickly outstrip the local resources available, particularly if current AA claimants rightly are protected. How would Councils restrict the way a non-means tested payment is given to older people locally to avoid busting their budgets? And how will Government avoid yet another driver of unequal treatment of older people in different parts of the country? The government rightly abandoned its plans to cut the Disability Living Allowance and unless there are good answers about the potential impact on older people's lives they should consider doing so too for the Attendance Allowance.

Thirdly, the devolution of responsibility and budgets for health and social care to some local areas offers the potential for a more holistic approach to be rolled out at a local level. DevoManc and other areas are seeking to grasp this opportunity in the hope that the advantages of local budgetary control, strong local relationships and a shared commitment to outcome-driven reform outweigh the risks of coping with massive reductions in funding at a time of rapidly growing demand and nationally imposed costs. But will they be given freedoms to diverge from national systems of funding formulas and tariffs, means tests and eligibility criteria, and governance rules and protocols in order to succeed? And do they have the ability to implement rigorous performance

management systems to ensure savings across the system are generated from reform and are spent in ways that ensure a financially sustainable system?

## Conclusion

If you view the world as half-full then the combination of devolution, NHS reform, the social care levy, AA reform, the Better Care Fund and the emerging evidence base of low-cost non-clinical solutions to high clinical care costs could provide some local areas with an opportunity to create a fundamentally different local health and social care system. But the risks are obvious when cash from central to local government is to be cut by £6bn (over 50%) over the next four years and the costs of care are due to rise from the national living wage without any funding to pay for it. Is the new care levy simply shifting the burden and politics of taxation from national income tax to local property tax rather than generating genuinely additional income?

To become sustainable, we need not only to reform the health and social care system, but to reform our thinking about that system. We should continue to look at value for money by shifting care from institutions towards the community, but we need to go a lot further, faster. Leaders of the health and care system must look beyond clinical solutions to reducing high clinical cost; must shift the system from being a 'sickness service' to being a 'health service' where we get serious about prevention; and must re-open the debate on a property-based care premium to meet the growing care needs of an ageing population in a fair and affordable way.

# A tale of two health systems

Sally-Marie Bamford, Director of Research and Strategy, ILC-UK

Kieran Brett, Director of Health at iMPOWER and former Special Advisor to the Secretary of State for Health

*Bob could not quite believe it had come to this – sixty six years of marriage, three children, two grandchildren, three family dogs and two cats; add in three house moves, not including his transfer to Melbourne in the 1980's and one modest win on the premium bonds (this led to their first peripatetic home or as Margaret liked to call it that 'sardine can on wheels'/caravan) – and he was now making what he felt was his 'last' move to 243 Lansdowne Road, Park View Residential Care. Meanwhile, Margaret was already at 24 Harborough Drive, otherwise known as the Oaks Nursing Home.*

*Bob was also minus one leg – thanks to diabetes or as he now believes thanks to poor medication management and foot care – and, as he was driven to the care home by his daughter, Jane, he also reflected perhaps thanks to a 26-year smoking habit. As a former Accountant, Bob always had a penchant for numbers, and after looking on the Diabetes UK website he wondered if out of the 135 diabetes-related amputations each week, 80 per cent of which could be avoided [122], he could, with the benefit of hindsight, have made it 134.*

*On the other hand, he didn't really see what he could have changed. If he added his vascular disease, renal and eye problems together with his diabetes, that equalled four health conditions to manage, which was four too many, particularly when he was trying to look after a wife with Alzheimer's disease. He had been coping when Margaret was well, he had to admit she always pestered him to go to the Doctors, take his medication and she did all the cooking…but things quickly changed.*

*As Margaret moved from early onset to the middle stages of the disease, Bob, despite his best efforts and putting Margaret's needs above his own, felt forced after a 'family meeting', that Margaret needed to go into a nursing home. After*

[122] Diabetes UK, https://www.diabetes.org.uk/About_us/News/More-than-135-diabetes-amputations-every-week/. Accessed 31st May 2016

*that it was all downhill for Bob...despite putting on some ad hoc Oscar winning displays of coping in front of the children and grandchildren, Bob just stopped caring and now if he added it all up, he had just far too many negative liabilities on his balance sheet.*

Of course it does not have to be like this, we know we can do better for Bob and so we should and indeed sometimes we do. The bigger question is why do we not do it the best way all the time? Our tale of two health systems will not linger on the "Worst of Times" but rather explore how we can create the "Best of Times" for Bob and others like him. We will also raise some challenges that may stop us getting there; to paraphrase Dickens, working to improve our health system will be a far, far better thing we do than we have ever done before. We are not in denial with regard to the scale of the endeavour; however, the NHS at its best is more than capable of recreating itself. Indeed many of the challenges we face are testament to the success of the NHS: the dramatic increase in average life expectancy arguably ranks as one of its greatest achievements. When the NHS was founded in 1948, the life expectancy for men was 66, and for women, 71.Today, current UK estimates for female life expectancy at birth are 82.8 years and 79.1 years for men.[123] The NHS has also shown its capacity for huge transformation and improvement in recent years. Remember when it took 18 months to get an operation or spending the whole day waiting in A&E to get seen. All transformed (although now starting to slip back). Treatments for the major 'killer' diseases radically improved and survival rates unrecognisable.

Without doubt the NHS is at a critical point in its history and in this essay we will explore how we can build on its achievements to deliver new models of care across the NHS. After a brief discussion of the founding principles of the Welfare State and the NHS, we will examine if today's NHS can meet our current health demands and if the Five Year Forward View[124] and the Transformation and Sustainability Plans[125] provide the right narrative structure for a bolder, brighter

[123] National Life Tables. United Kingdom, 2012-2014. Office for National Statistics, 2015

[124] The NHS Five Year Forward View was published on 23 October 2014 and sets out a new shared vision for the future of the NHS based around the new models of care. It has been developed by the partner organisations that deliver and oversee health and care services including Care Quality Commission, Public Health England and NHS Improvement (previously Monitor and National Trust Development Authority).

[125] In December 2015, the NHS shared planning guidance 16/17 – 20/21 outlined a new approach to help ensure that health and care services are built around the needs of local populations. To do this, every health and care system in England will produce a multi-year Sustainability and Transformation Plan (STP), showing how local services will evolve and become sustainable over the next five years – ultimate-

future 'tale' for Bob.

Were Beveridge to report back on progress today in slaying his five Giant Evils of *Want, Ignorance, Idleness, Squalor and Disease*, he would certainly have much that is positive to say on the latter. However, he would perhaps challenge us on progress on a key underpinning assumption about the extent to which the NHS has proactively prevented short-term injuries from becoming long-term disabilities. His whole model of welfare was premised, in part, on this. Citizens had a duty to get themselves well as quickly as possible and so cease to be a cost to the public purse. To help them achieve this objective, the NHS was not to become an ill-health service.[126] It was also based on three key foundations: it meets the needs of all citizens, it is free at the point of delivery and it is based on clinical need, not the ability to pay. As the NHS approaches its 70th birthday, this generation of leaders now have the formidable task of preserving and protecting those principles. Done badly, these principles could be breached. This will mean cuts in services, and consequently, unnecessary suffering often affecting those who need the NHS most and a risk of flight by those who can afford it. Done well, it will mean better outcomes; less suffering; fewer years lost to life limiting illness and lower costs. Arguably we can do this, but the pace needs to quicken and the centre will need to use its levers to accelerate the rate of change.

In October 2016, we will be two years into the Five Year Forward View. Simon Stevens, the head of the NHS in England, in his 'manifesto' for the health service concluded that: "*The NHS cannot achieve this alone: bending the curve on ill health will require concerted action from individuals, local government and other public, private and third sector bodies alongside the health service*" [127]. And indeed during the past two years, new models of care have begun to emerge and there are exciting examples of real change that would give Bob a better life, in particular the creation of 44 Sustainability and Transformation Plans (STPs) with the associated plans that are being developed as we speak. STPs create the possibility of generating change across larger areas. The key challenge will be how STPs can generate real traction on the ground amongst a

ly delivering the Five Year Forward View vision of better health, better patient care and improved NHS efficiency.

[126] Field F. Nov 2012. New Statesman, http://www.newstatesman.com/politics/politics/2012/11/cradle-grave Accessed 1st May 2016.

[127] NHS. Five Year, Forward View: Time to Deliver. 2015

complex set of local relationships. NHS England, NHS Improvement and Public Health England can learn much from the history of partnership working – for good and ill.

Public Partnerships have failed as often as they have succeeded. Why? There are a number of reasons. Firstly, partnerships are created to tackle problems that are bigger than any single organisation but organisations are created to do very specific things, often in a specific framework of rules. The terms of authorisation for Foundation Trusts (FT) are a good example. Why would the Board of an FT seek to breach the set of rules it was set up to deliver? Secondly, people work in organisations and feel they are the unit that they belong to. Partnerships can feel nebulous, distant and unconnected. Loyalty to 'where I work' can seem more attractive than working in new ways to deliver new models of care. Thirdly, people have grown weary of new initiatives, even if they are good initiatives.

So what does this mean for STPs and more importantly Bob? We know that partnerships can work very effectively. The best Local Strategic Partnerships; Crime and Disorder Partnerships and Drug Action Teams, one could argue delivered some long lasting and strong results. However, they often need support, resources, and where necessary, central pressure to deliver. The national organisations need to get this balance right. Some of the early signs are positive. Nearly every STP area has a nominated lead and a responsible officer and the STP process is backed by significant resources. The new Clinical Commissioning Group (CCG) performance assessment regime requires close partnership working and the STP process will be backed by a strong central response where progress is not strong enough.

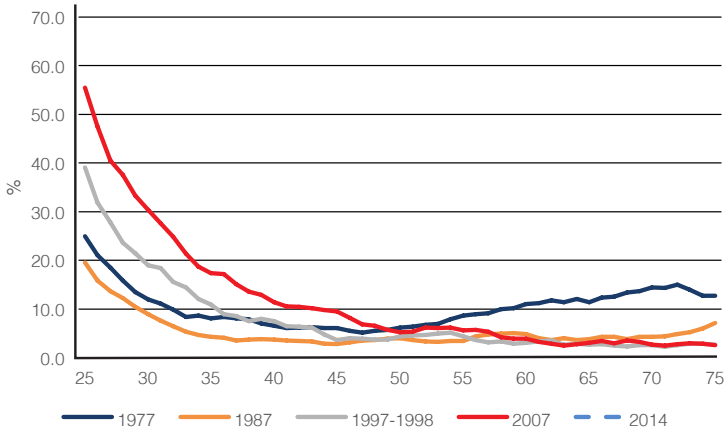
However, the challenge is to balance complexity and pace. National support will need to be shaped to help areas get furthest fastest, but some risk-taking and freedom will be a key element of success. For example, there will inevitably be a period of double-running as new models of delivery are developed and existing models remain in place. This may mean allowing providers to go into managed deficits until upstream prevention can start delivering results. That in turn means ensuring that improvement plans for providers this year contain a strong emphasis on part-funding preventative care models which in time will allow the acute sector to reduce in scale. If NHS England and NHS Improvement can prove to the Treasury that this will be a temporary state of affairs, then

they gain more headroom and prevent a second year of using the STP fund to prop up the current system. This tension between stability and change will become abundantly clear in this financial year. The risk is that change loses out and the noble aims of the Five Year Forward View will begin to come under strain. Disruption is disruptive by definition. It means a bit of a mess for a while. Admitting that stability could be the enemy of change and quantifying what that means for NHS providers could be a much more productive way to deliver the new NHS.

Why does this matter for Bob? Yes, there have been huge improvements in our NHS but our challenge now is to help make sure that Bob and all those like him do not face the 'worst of times.' The current ambitious reform agenda needs to be backed by political courage and much greater acknowledgement that provider deficits should be addressed by dealing with the wider demand pressures in every health economy. If 'sustainability' is allowed to triumph over 'transformation' then we will be back counting deficits next year and the year after that. The new models of care and STPs are the right way to go. There is also an opportunity for Simon Stevens to put 'rocket boosters' under is his ambition to see 'north of five million people on personal health budgets', because right now there are many Bobs out there who are not offered them. Personal Health Budgets combined with the new integrated care models perhaps offer an exciting and potentially rapid route to achieving a genuinely transformed NHS.

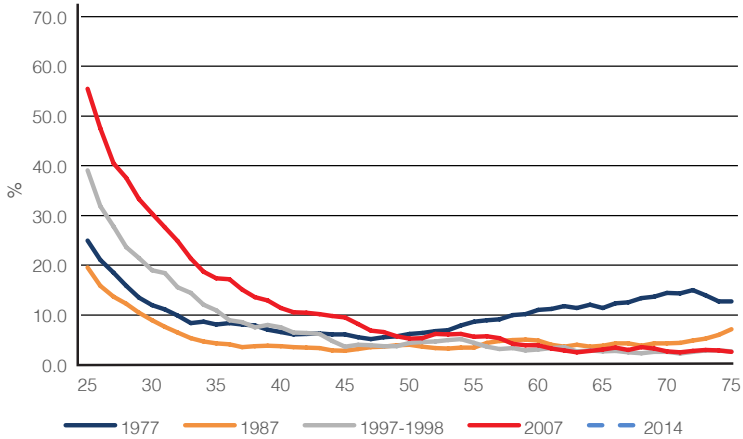
The politics and narrative of transformation need to be better articulated. It cannot and should not be seen as way to deal with a managed decline in the proportion of national income that we spend on the NHS and social care. There are big choices to be made on those questions and we will need to confront them. The reductions in social care budgets are now feeding into real system problems, including access to residential care or alternative post-hospital care for older patients. These will have to be tackled and spending will eventually need to rise. However, that is not an argument in defence of what we do now. Bob does not need to worry about delivery and transformation, but new models of care should be described as better models of care because they will look after Bob more effectively. Bob need not have suffered so much: he could have lived, supported with his wife, Margaret for longer in their own home - that would have been Bob's preferred 'tale' for his health service. Imagine what we could do in the future.

## Proportion of individuals by age and housing tenure, rolling five year age groups, UK (private rentals)




Source: ONS

## Proportion of individuals by age and housing tenure, rolling five year age groups, UK (mortgage households)

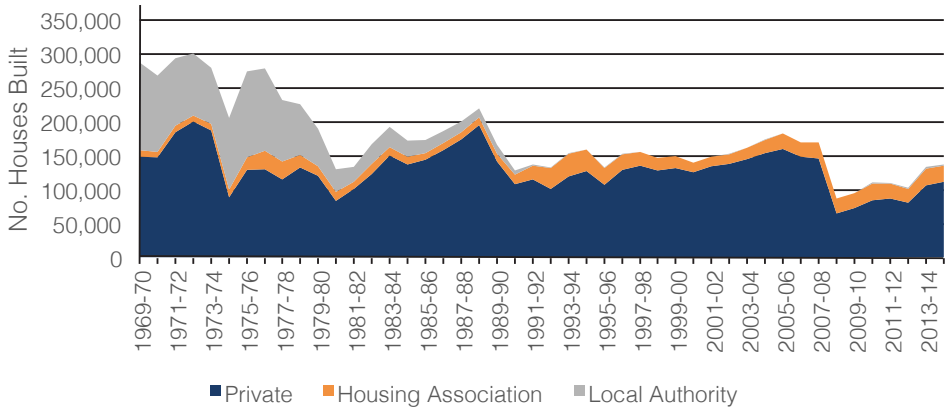



Source: ONS

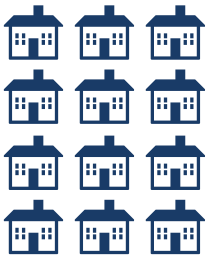

**In 1987, 19% of people** between the ages of **16-24 lived in private rented accommodation** and **49% lived in a mortgaged house.**

**By 2014, 62% of people** between the ages **of 16-24 lived** in privately rented accommodation and **15% lived in a mortgaged house.**

## England housebuilding (permanent dwellings), stacked by tenure




Source: DCLG



**In 1969-1970,** local authorities were responsible for over a **100,000 homes being built**, but this **number collapsed by 1989-1990.**

**In 2013-2014 less than 150,000 new homes were built,** compared to a peak of **nearly 300,000 new homes in the 1970s.**

# How a greater focus on 'last time buyers' and meeting the housing needs of older people can help solve the housing crisis[128]

Sir Michael Lyons, non-executive chairman of the English Cities Fund and Participle Ltd; and author of the Lyons Housing review

Caroline Green, Assistant Chief Executive Oxford City Council and worked on the Lyons Review

Neal Hudson, Associate Director of
Savills Residential Research and worked on the Lyons Review

## Introduction "The paradox of housing the young"

One of the key challenges facing the nation is the need to tackle the continuing housing crisis. The consequences of failing to build enough homes for decades are already keenly felt by millions of people and have wider effects on the management of the whole economy.

One in four adults between the ages of 20 and 34 are still living with their parents. This is hardly surprising when the typical first time buyer needs a deposit equal to 65% of their income and the average household spends 40% of their income on rent.[129] We have the bizarre situation in which a generation of graduates who have benefited from the significant investment in high quality student housing in recent years, now find themselves forced into lower quality accommodation and living conditions as they begin their working lives, as a result of the high cost of housing and substantial student debts.

[128] This contribution builds on the findings of the Lyons Housing Review (2014): Mobilising across the nation to build the homes our children need: http://www.yourbritain.org.uk/uploads/editor/files/The_Lyons_Housing_Review_2.pdf
[129] ONS, Young Adults living with parents, 2013; of Mortgage Lenders, Helping the Bank of Mum and Dad, 2013; English Housing Survey, 2012/13

## Housing reform

The need to build more homes has at last become a priority for Government and it is now focusing its efforts on 'first time buyers', particularly through the starter homes initiative, which is set to displace support for any other affordable housing[130]. However, in this article we introduce the "paradox of housing the young" and argue that faster progress may be made in helping young homemakers and in building a sustainable increase in the supply of new homes if we devote as much of our energies to meeting the housing needs and aspirations of their parents and grandparents.

### Why older people?

The political and policy focus on first time buyers is a legitimate response to the expressed ambitions of homeownership by younger generations, however the major drawback is that it concentrates on a part of the population with weakest effective demand. Older home owners, by comparison, have much higher levels of housing wealth and therefore represent a much more reliable source of effective demand for new homes provided those homes meet their aspirations. Many are also less likely than younger generations to need public support in the form of Rent to Buy or Help to Buy (which is not to say they won't take advantage of such schemes when able!). Collectively this age group are sitting on over £1 trillion worth of housing equity[131] and there is evidence of a growing appetite amongst this generation for equity release. A record amount of housing wealth was unlocked by homeowners aged 55 and over in 2015. Lending was up 16% on 2014 with £1.61bn withdrawn through specialist equity release plans[132].

Focusing on the housing needs and aspirations of older people makes a direct contribution to meeting the housing needs of other parts of the population. In particular, it can support families to move into currently under-occupied homes. The London Assembly identified that freeing up a six bedroom house would free up housing for 36 people through unlocking the housing chain[133]. In addition by releasing capital, older home owners can support children and grandchildren who cannot currently access their own home. There is no suggestion here of compelling people to sell their homes and, of course, the opportunity for equity

[130] Inside Housing, Starter Homes to eat up affordable housing supply, May 2016
[131] ONS op cit
[132] http://www.theguardian.com/money/2016/jan/25/equity-release-levels-record-high-2015-over-55s
[133] London Assembly Planning and Housing Committee, Crowded houses Overcrowding in London's social rented housing, 2011

release does not exist for all families or in all areas of the country. However, the imbalance of housing wealth between generations means that more families may already be looking for solutions that enable some of that housing wealth to be shared with children or grandchildren.

The term "older people" conceals a wide diversity of incomes, and aspirations, lifestyles and cultures and a spectrum of care needs, all leading to interest in different housing options. Catering to the aspirations of older people in addition to a focus on meeting their needs will be crucial to developing homes that encourage more to downsize. Other studies have explored motivations for and barriers to downsizing[134] which we do not have room to explore here, but can be broadly grouped into three main categories of motivation for downsizing:

- Needs based downsizing – driven by the need to move to a smaller home as a result of bereavement, isolation, inability to manage and maintain a large family home, or poor health, mobility or care requirements that require adapted properties of a greater level of home based support.
- Economic based downsizing - older people with fixed or declining incomes have an interest and an incentive in reducing housing running costs from moving to a smaller or more efficient home, or they may look to free up equity in order to afford a better standard of care or to support their children in accessing a home.
- Aspirational downsizing – typically at the younger end of the age range in 60s or 70s whose children have left home and who may be looking to free up equity and have an "easier to manage" home that allows them to pursue "new life adventures" such as travel, education and leisure activities.

## Meeting the needs of potential downsizers

The biggest challenge and opportunity is in delivering an aspirational product that encourages people to downsize at a price that they can afford within a model that works for house builders, developers and investors.

Meeting this challenge will require us to think more creatively about homes for older people. Bungalows are often considered the most popular home among older people and are the solution that politicians and policymakers typically turn to when thinking about homes for older people. However, they are often inefficient in terms of land use and the values they achieve reflect the underlying

[134] See for example Demos, Top of the Ladder, 2013; JRF *Managing Resources in Later Life* 2009

development value of the land rather than the bungalow, making them an expensive option. It will be important therefore to find ways of translating the features that make them attractive, such as plenty of space, storage, and access to outside space, to new developments that make more efficient use of land.

Increased competition in this area, with an emphasis on higher density developments and with greater attention to the quality of build and place might help to bring costs down, increasing the viability of such developments. In view of the fact that older people tend to favor living as part of wider communities rather than segregated retirement settlements, there are opportunities to ensure that new communities, for example Garden Villages and urban extensions, include the type of development that will be attractive to older people. In some urban areas high rise apartment blocks have enjoyed consistent popularity with older tenants.

The increased opportunities for self-build, or self-commissioning that Government is currently promoting could be targeted to downsizers. They represent a potentially attractive option for those who have equity but feel there is a lack of choice to meet their aspirations or those for whom retirement settings do not appeal. The opportunity to design and specify their own home offers a means by which people can cater for current lifestyle choices and potential longer term needs.

Shared ownership schemes offer a means to encourage downsizing for older people who cannot afford the full market price of a new home or wish to free up capital with the attraction of continuing to own their home. Many Housing Associations offer schemes specifically designed for the over 55s providing a means for them to buy a stake in a new retirement home without overstretching themselves financially or tying up all their money in their home. Government's recent announcement of the expansion of support for shared ownership schemes offers potential to promote this as an option more widely to older people and stimulate demand.

As the CIH have illustrated, new models are emerging that are focused on providing high quality accommodation, built to HAPPI standards[135] , but without the support traditionally associated with retirement housing[136]. This is partly in

[135] 104. "Housing our Aging Population: Panel for Innovation (HAPPI)", DCLG 2009
[136] CIH, New approaches to delivering better housing options for older people, 2015

response to reduced funding and the high costs and difficulties associated with extra care developments, but also in recognition that a more attractive offer would encourage more people to actively plan for their future housing needs. L&G have also identified capacity for greater investment in retirement homes for sale in recognition of opportunities for equity release if demand could be mobilised[137].

Finally, a greater focus on "future proofing" new houses to "lifetime standards" so that they can be adapted as lifestyles, mobility and support needs change would provide additional choice to bespoke housing for older people and increase its attraction for those looking to downsize. Currently only 3.4% of homes have the four basic recommended features to enable someone with mobility problems to visit let alone reside (level access, flush threshold, WC at entry level and circulation space).

## Unlocking the potential requires increased supply

Unlocking these benefits will require a better housing offer for those 'last time buyers'[138] looking to downsize to a home that better suits their needs and aspirations and releases capital tied up in larger homes.

However, the solution is not just about home ownership. We will also need a wider array of homes for rent in purpose built and well managed settings with secure tenancies, recognizing the unmet housing need of a growing elderly population without capital or access to mortgages. As home ownership becomes increasingly unaffordable for people in their 30s, 40s and beyond, the proportion of older people renting privately is likely to grow significantly.

A better rental offer with secure tenancies and confidence of rent stability might also provide an attractive offer for home owners looking to release capital to provide an income in later years and to help fund housing for their children and grandchildren. Crucially, stimulating the market for rented homes will deliver a faster increase in housing supply. This is because building homes to rent offers the opportunities for quicker build out, bringing in a wider range of commissioners of housebuilding, enabling greater density of development and

[137] Legal & General Let's House Britain, 2014

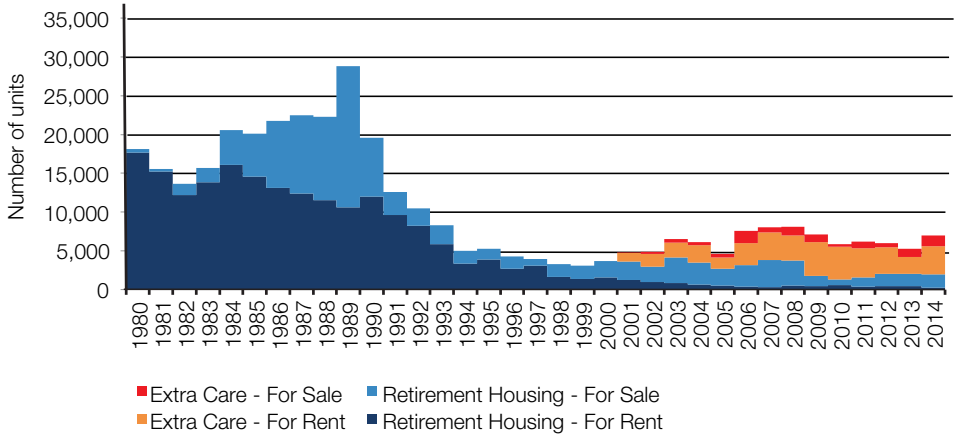
[138] 'Last time buyers' was a working term we used during the Lyons review to refer to the group of people who want, need and aspire to buy a different type of home suitable for later stages in life. Whilst we never felt quite comfortable with some of the connotations of the phrase, we never found an alternative that could succinctly capture the issue and so the phrase has stuck.

greater scope for the use of modern manufacturing methods which can enable faster build and address constraints on materials supply to increase capacity for house building.

## How many homes are needed?

We are arguing in this article for a wider choice for older house buyers but the stock of homes specifically designed for the elderly is already limited. There are around 515,000 specialist retirement and extra care homes in England[9.] Supply of new homes specifically for older people has averaged around 7,000 units per year over the last decade. This equates to a 1.4% increase in existing stock - around double the level being achieved by the general new build housing market although significantly below levels achieved in past decades and way behind the level needed to match our aging population. [139].

### Delivery of housing for older people



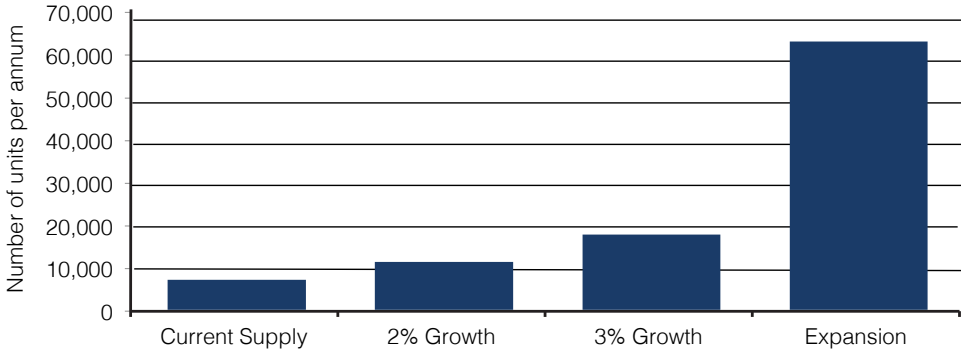

Source: Elderly Accommodation Council

The Joseph Rowntree Foundation have identified that there is only enough specialist housing to accommodate 5% of the over-65 population.[140] Analysis by Savills suggests that in terms of housing need, the projected 2% annual increase in the number of people over 65 between 2015-2020 and the 3.2% increase in the number of people over 75 would suggest a target of 18,000

[139] Housing LIN, Will the Private Extra Care Housing Market take off in 2014? 2014
[140] Joseph Rowntree Foundation, Supported housing for older people in the UK: an evidence review, 2012

homes per annum are needed to maintain existing provision. Increasing the provision of retirement homes to 10% of older people would require an additional 60,000 homes per year above these levels[141].

**Future housing requirement**




Source: Savills Research

## How can we build more homes?

There is clearly an appetite and opportunity to increase the contribution made by house builders and others to the supply of homes that are attractive and suitable for older people. Promoting a greater understanding and assessment of market opportunities and finding ways of supporting demand will help to drive up supply and mobilise the current efforts of specialist developers. However, we will not build the number or mix of homes we need if we rely on the existing industry alone to build them. For that, we will need a range of organisations including housing associations, local authorities and regeneration agents, to play a much greater role in commissioning housing.

The traditional model of the volume housebuilders is focused on building homes for sale and, despite the benign conditions being created for the industry and the corresponding increase in output, there are limits on the rates at which house builders build out their sites. Although some house builders are committed to continuing growth, the rate of housebuilding is dictated by demand for the finished houses being at a level that meets the return on capital that the volume house building model requires. The history of the last 30 years has shown that industry output closely follows the economic cycle with capacity contracting

[141] Savills Spotlight Housing and Ageing Population, 2015

with each downturn and peak. Government may exacerbate this problem by focusing so firmly on its starter homes initiative which involves highly focused subsidies and seems set to displace other affordable housing.

Investment in homes for rent, both at market and sub-market rent in addition to support for homeownership can play an important role not only in meeting local needs, but also in driving up overall build rates and providing some insulation in counter-cyclical periods. The fact that homes built specifically for rent do not compete with the traditional developer business core model of building homes for individual buyers, means there is a significant opportunity to increase the number of homes built. There is evidence of untapped potential for large scale institutional investment in the private rented market as can be seen from Legal and General's recent decision to invest £600 million in building over 3,000 apartments for rent. Stimulating the market for rented homes offers the opportunities for quicker build out, bringing in a wider range of commissioners of housebuilding, enabling greater density of development and greater scope for the use of modern manufacturing methods which can enable faster build and address constraints on materials supply.

## An expanded role for local authorities and housing associations

We will need local authorities and housing associations to greatly expand the role they play in commissioning homes aimed at older people. There are significant challenges arising from government social housing policies which will need to be overcome, including the impact of the reduction in social rents and the extension of Right to Buy which are impacting on councils' and housing associations' plans for investment in housing[142]. The government has now announced a 1 year exemption for supported housing from the social rent reduction, recognising the significant impact it would have on the provision of new retirement housing schemes. However the on-going uncertainty about what will happen in future years will continue to impact on investment plans[143]. In addition to the overall impact on council housing stock, the requirement for councils to sell high value council homes to pay a levy to fund the extension of the Right to Buy could have a disproportionate effect on homes for older

[142] The LGA estimates that the Government's housing policies could result in the loss of 80,000 council homes http://www.local.gov.uk/media-releases/-/journal_content/56/10180/7668062/NEWS

[143] Inside Housing January 2016 http://www.insidehousing.co.uk/supported-housing-wins-one-year-rent-cut-exemption/7013708.article

people.[144]

Government needs to ensure the important contribution that both local authorities and housing associations can play alongside the private sector is reflected in their policies. As a country we have only ever managed to build the number of homes we now need when the public sector has funded a significant number of them and in recent years housing associations have been key delivery agents. Finding ways in which local authorities can promote, support, finance and commission new homes and giving housing associations the certainty they need and the ability to plan long term will be critical to achieve the Government's housebuilding targets and in ensuring greater commissioning of homes suitable for older people. The Government's renewed determination to releasing surplus public land, most recently highlighted in the Chancellor's 2016 Budget Statement[145] provides an important opportunity for a great deal more housing of a range of types that are suitable and adaptable for older people which could be brought forward as part of inclusive communities. Making this a priority for NHS surplus land in close proximity to continuing health facilities might be a first move. It is crucial therefore that in implementing its public land policies, Government allows these opportunities to be captured rather than simply releasing land without concern for the end product. Government has taken initial steps towards this with announcement of pilots for direct commissioning on public land. An expanded and more ambitious approach to greater direct commissioning would allow councils and housing associations to specify the type and standard of homes to increase supply of homes with older people and downsizers in mind.

## Conclusion

A new and increased emphasis on meeting the housing needs and aspirations of the older house buyers offers the opportunity to unlock a bigger and more secure market for newly built homes. Paradoxically, a closer policy focus on housing provision for older people is an effective way to help the housing needs of the younger generation. It would free up much needed family homes and stimulate movement across the housing chain. It would also offer a means of addressing the imbalance of housing wealth between the generations by

[144] JRF, Great British Bungalow sell off 2016 https://www.jrf.org.uk/press/great-british-bungalow-sell-1-4-forced-council-house-sales-could-be-bungalows

[145] The 2016 Budget announced that Local Authorities will collaborate with central government and partners to release land with the for at least 160,000 homes. HM Treasury Budget 2016

enabling parents and grandparents to release capital to help their children and grandchildren to access their own home. In addition, providing new homes that can better address the housing needs of the elderly would reduce the burden on health and care services and help people to remain independent and in good health in their own homes. Unlocking these benefits will require a better housing offer for older people, across a range of tenures, that provides homes that better suit their lifestyle, needs and aspirations.

# Housing our ageing population: the role of the state

Lord Richard Best

As we get older our housing needs change. The space we required for a growing family, indoors and out, is no longer a necessity – and it may well become a burden. Steps and stairs can become a liability. The cost of heating and maintenance can undermine our standard of living.[146]

Care and repair schemes operated by home improvement agencies can enable older people to adapt their homes and stay put, sometimes helped with Disabled Facilities Grants from the local authority.[147] It can be sensible for older home owners to withdraw equity tied up in their property to pay for improvements which make that property more comfortable. But this approach will not always be feasible or achieve a lasting solution.

At the same time, many of us become prone to loneliness in older age. We have less reason to get out and about and our social life gets narrower. Isolation can undermine our health and well-being.[148]

Meanwhile for the nearly three quarters of us who are home owners, much of our wealth is tied up in our property.[149] If we were to need resources, for

[146] *HAPPI: Housing our Ageing Population: Panel for Innovation,* Homes and Communities Agency (2009), p.11. https://www.gov.uk/government/uploads/system/uploads/attachment_data file/378171/happi_final_report_-_031209.pdf John Hills, *The Hills Fuel Poverty Review* (2012), p.7-8. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/48297/4662-getting-measure-fuel-pov-final-hills-rpt.pdf Age UK, *Older, not colder: Why older people need warm homes* (2014). http://www.ageuk.org.uk/Global/STW/STW%202014/LR_ID202086_Warm_Homes_%20report_24pp_2014_SPREADS.pdf?dtrk=true

[147] The All Party Parliamentary Group on Housing and Care for Older People, *Living Well at Home* (2011). http://www.housinglin.org.uk/_library/Resources/Housing/Support_materials/Other_reports_and_guidance/living-well-at-home.pdf Sue Adams, Care and Repair England, *A Perfect Storm: An ageing population, low income home ownership, and a decay of older housing* (2010).

[148] Office for National Statistics, *Insights into Loneliness, Older People and Well-Being,* (2015), p.6. http://webarchive.nationalarchives.gov.uk/20160105160709/http://www.ons.gov.uk/ons/dcp171766_418058.pdf Louise Bazalgette and Jo Salter, Demos, *The Hanover @ 50 debate: Sociable housing in later life* (2013), p.5. http://homeshare.org/wp-content/uploads/2012/04/Sociable-Housing-in-Later-Life-May13.pdf Dr Samantha Callan, The Centre for Social Justice, *The Hanover @50 debate: Strengthening relationships to prevent isolation and loneliness in old age* (2013), p.9. http://www.centreforsocialjustice.org.uk/UserStorage/pdf/Pdf%20reports/CSJ-full-think-piece.pdf

[149] Claudia Wood, Demos, *The Top of the Ladder* (2013), p.37. http://www.demos.co.uk/files/Topoft-heLadder-web.pdf?1378922386 International Longevity Centre – UK, *Generation Stuck: Exploring the Reality of Downsizing in the UK* (2016), p.4. http://6c6ad24b91280faab9ef-a33e598b21c2445c4e-

example to cover care costs or to help our children/grandchildren, we probably need to release some of these funds.[150]

## To downsize?

It is easy to say that the answer is to downsize to a more suitable place – somewhere easy to manage, with enough space and light, perhaps with companionship on tap – and take out some cash at the same time.[151]

But few of us in the UK – unlike our counterparts in continental Europe and North America – take the plunge and "right-size" when we are in our "extended middle age.[152] We await the health crisis or bereavement that forces us – or our children on our behalf – to look for somewhere more suitable: and, at that stage and under pressure, we are unlikely to end up where we would like to be.[153]

This attitude to our housing is not serving us well. It means that in place of a rewarding retirement, lots of older people are living uncomfortable and lonely lives, sometimes facing the miseries of cold and ill-health.

## The intergenerational dimension

At the same time as nearly seven million properties with more than two spare rooms are occupied by those over State Pension Age, younger families find it harder and harder to afford the space they need.[154] Over one million live in

ca86a9b4f92e58.r96.cf3.rackcdn.com/ILC-downsizing-report.pdf

[150] *HAPPI: Housing our Ageing Population: Panel for Innovation,* Homes and Communities Agency (2009), p.18. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/378171/happi_final_report_-_031209.pdf

[151] Hackett, P. and Hunter, P. (2013) The Smith Institute, *The Hanover @ 50 debate: Selling off the family silver* http://www.erresearchcentre.org/wpcontent/uploads/2013/05/Smith-Institute-equity-release-April-2013-2.pdf International Longevity Centre (2016) – UK, *Generation Stuck: Exploring the Reality of Downsizing in the UK*, p.11. http://6c6ad24b91280faab9ef-a33e598b21c2445c4eca86a9b-4f92e58.r96.cf3.rackcdn.com/ILC-downsizing-report.pdf

[152] Best, R, (2013). *The Hanover @ 50 debate: Accommodating our Extended Middle Age*
*HAPPI,* (2009). *Housing our Ageing Population: Panel for Innovation*, Homes and Communities Agency https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/378171/happi_final_report_-_031209.pdf Shelter, (2012). *"A better fit? Creating house choices for an ageing population"* p.13. https://england.shelter.org.uk/__data/assets/pdf_file/0005/427730/Policy_report_A_better_fit.pdf Leach, J, (2012) "The Intergenerational Foundation, Understanding Downsizing", p.10. http://www.if.org.uk/wp-content/uploads/2012/04/Understanding-Downsizing-Why-People-Choose-to-Downsize-or-Not.pdf

[153] Wood, C. (2013), Demos, *The Top of the Ladder* p.34. http://www.demos.co.uk/files/TopoftheLadder-web.pdf?1378922386

[154] Legal and General (2015),, *Last Time Buyers* p.2. http://www.legalandgeneralgroup.com/assets/portal/files/pdf_175.pdf Griffith, M., (2011). The Intergenerational Foundation, *Hoarding ofHousing* http://www.if.org.uk/wp-content/uploads/2011/10/IF_Housing_Defin_Report_19oct.pdf Morton, A. (2013). Policy Exchange, *The Hanover @ 50 debate: Housing and Intergeneration Fairness* http://www.policyex-

seriously over-crowded conditions.[155] Too many children miss out on even the smallest of gardens. Too many parents hardly see their children because they have to commute so far to give them a decent environment. And many others postpone having children at all because they cannot afford a decent home for them.[156]

The answer, for young and old alike, lies in a better match of homes to households. If only those with properties that will become increasingly burdensome were to move to tailor-made "age-friendly" new homes, the disastrous housing situation facing the under 40's could be eased.

## Why the housebuilders are failing us

But no-one is going to move if there is nothing on the market that matches their needs and aspirations. Without the choice of an attractive alternative to staying put, all of us will simply dig in and await the crisis that compels us to leave.[157]

Sadly, leaving the job to the market is not working. Despite the huge potential and enormous purchasing power of late middle-agers, the house-builders are not entering this market on any scale. Why not?

Building for down-sizers is costlier than for first-time buyers (or buy-to-let investors). The older buyer will be spending far more of their time in the home; they are not going to settle for the lack of space and low standards which young people – out all day at work and play – can tolerate. Good design – better space and accessibility, no stairs, walk-in showers, etc. – adds a bit to the build costs.[158] And if the age-exclusive development has any shared areas, such as

change.org.uk/images/publications/housing%20and%20intergenerational%20fairness.pdf

[155] Office for National Statistics (2014), *Overcrowding and Under-occupation in England and Wales* p.1. http://webarchive.nationalarchives.gov.uk/20160105160709/http://www.ons.gov.uk/ons/dcp171776_360082.pdf

[156] Morton,A. (2013) Policy Exchange, *The Hanover @ 50 debate: Housing and intergenerational fairness,* p.3. http://www.policyexchange.org.uk/images/publications/housing%20and%20intergenerational%20fairness.pdf Shelter/ YouGov, Poll (March 2015). http://england.shelter.org.uk/news/march_2015/parents_delaying_having_children_because_of_sky-high_housing_costs

[157] Jenny Pannell, Hannah Aldridge and Peter Kenway, Joseph Rowntree Foundation, *Older People's Housing: Choice, Quality of life and Under-Occupation* (2012), p.3-4. https://www.jrf.org.uk/file/41967/download?token=3zBs9lGG&filetype=findings International Longevity Centre (2016)– UK, *Generation Stuck: Exploring the Reality of Downsizing in the UK*, p.4. http://6c6ad24b91280faab9ef-a33e598b21c2445c4eca86a9b4f92e58.r96.cf3.rackcdn.com/ILC-downsizing-report.pdf Wood, C. (2013), Demos, *The Top of the Ladder*, p.34. http://www.demos.co.uk/files TopoftheLadder-web.pdf?1378922386

[158] The All Party Parliamentary Group for Housing and Care for Older People (2014), *The Affordability of Retirement Housing* p.26-27. http://www.demos.co.uk/files/Demos_APPG_REPORT.pdf?1415895320

a "club room" or some communal garden, the extra costs must be added to the price. Service charges for ongoing management and maintenance expenses will be higher: although these pooled costs for new apartments will actually represent much lower outgoings than for the previous property, they can be off-putting to buyers.[159]

These factors make the product more difficult to sell profitably. Good marketing skills could secure the necessary additional price for the additional value; but there are few specialist developers with this expertise.

## The role of the state

So does the State have a role in kick-starting the cultural change to get the UK to the tipping point where right-sizing becomes the norm for all of us in our extended middle age?

Governments certainly have big incentives to intervene. The NHS faces ever-growing expense from admissions caused by accidents and falls in the home; and from the bed-blocking by patients who can't be discharged back to unsuitable properties, or who are quickly re-admitted because they cannot cope with the conditions when they are sent home.[160] And this country's poor record on premature winter deaths is a barometer of the problems created by cold and damp properties.[161]

For local authorities, many of whom are facing a cost crisis for their adult care departments, spending on domiciliary services is inflated by problems of supporting people in unsatisfactory conditions.[162] And unnecessary moves into

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[159] The All Party Parliamentary Group for Housing and Care for Older People, (2014) *The Affordability of Retirement Housing*, p.29-31. http://www.demos.co.uk/files/Demos_APPG_REPORT.pdf?1415895320

[160] Care and Repair England, *If only I had known: Integration of housing help into a hospital setting* (2016), p.6. http://careandrepair-england.org.uk/wp-content/uploads/2014/12/If-Only-I-Had-Known-Local-Projects.pdf Lord Carter of Coles, Department of Health, *Operational Productivity and Performance in English NHS acute hospitals: Unwarranted Variations* (2016), p.64-68. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/499229/Operational_productivity_A.pdfBest, R. (2013), *The Hanover @ 50 debate: Accommodating our extended middle age*, p.13.

[161] Office for National Statistics (2015), *Statistical Bulletin: Excess Winter Mortality in England and Wales: 2014/15 (Provisional) and 2013/14 (Final)*. http://www.ons.gov.uk/peoplepopulationandcommunity/birthsdeathsandmarriages/deaths/bulletins/excesswintermortalityinenglandandwales/201415provisionaland201314final Marmot Review Team (2011), *The Health Impact of Cold Homes and Fuel Poverty*. https://www.foe.co.uk/sites/default/files/downloads/cold_homes_health.pdf

[162] Local Government Association/ Association of Directors of Adult Social Services (2014), *Adult Social Care Funding: 2014 State of the Nation Report*, p.6. http://www.local.gov.uk/documents/10180/5854661/Adult+social+care+funding+2014+state+of+the+nation+report/e32866fa-d512-4e77-9961-8861d2d93238

residential care are a ridiculous expense for all parties – and hugely unpopular with older people themselves.[163]

At the same time, local and central government is now seized of the necessity to generate more homes for the next generation. Freeing up family housing (often with gardens) unlocks three or four moves in the property market with very positive economic effects.[164] The objections to all home-building – the so-called NIMBY problems – are likely to be far more muted when the new homes are for older people who will, no doubt, be good neighbours and will generate less traffic and noise.[165]

On every count, the State, nationally and locally, has good reason to promote new housing for those over State Pension Age. So what form could public intervention take to scale up the creation of high-quality homes for this demographic?

## Five forms of state intervention

First, there is the need for advice. Government is taking seriously our need to get guidance before cashing in our pension pots. Websites and free personal consultations are now available.[166] But advice on how to treat the – usually much larger – asset of our own home, is harder to come by. Before down-sizing, older people need to understand the tax and benefit position they will face; or before deciding to take out equity release mortgages or other financial products, all the implications need to be explained. It would be worth central government putting some modest funding into an extension of the current advisory services.[167]

Second, the transactional costs of making a move can be a barrier: removal of Stamp Duty Land Tax for those over State Pension Age could be a valuable sweetener. And because of the chain reaction from one down-sizing move,

[163] Best, R (2013), *The Hanover @ 50 debate: Accommodating our extended middle age*, p.13-14. A Cebr Report for Killik & Co, (2015) *The cost of care in later life*, p.4. https://www.killik.com/documents/cost-of-care-report-2015/

[164] *HAPPI, (2009) Housing our Ageing Population: Panel for Innovation*, Homes and Communities Agency, p.18. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/378171/happi_final_report_-_031209.pdf Legal and General, (2015), *Last Time Buyers*, p.2. http://www.legalandgeneralgroup.com/assets/portal/files/pdf_175.pdf

[165] Lyons, M (2014), The Lyons Housing Review. *Mobilising across the nation to build the homes our children need*, p.135-138. http://www.yourbritain.org.uk/uploads/editor/files/The_Lyons_Housing_Review_2.pdf

[166] http://www.pensionsadvisoryservice.org.uk/

[167] http://www.firststopcareadvice.org.uk/

Treasury would be likely to gain handsomely from such a concession.[168]

Third, there is the problem of the affordability of down-sizer homes for those with less valuable houses to sell. If the home-owner cannot raise enough from the current property to pay for the new one, the gap needs to be bridged. The shared ownership model can achieve this, with or without an element of rent being payable for the percentage of the equity that is not purchased with the sales proceeds. Alternatively, the current Help to Buy scheme for first-time buyers could be utilised to cover "last-time buyers" – assisting the first-timers in the process – with an interest free equity loan (well-secured by the owner's own equity share).[169]

Fourth, the planning system could be used to incentivise new house-building for this market. The Starter Homes initiative aims to get developers building homes for sale at a 20% discount to the under 40's: an exception or extension of this initiative could encourage new provision for the over 60's (or for those over State Pension Age). Bringing family homes onto the market – some of them in need of the upgrading which younger buyers have the energy to undertake – would help both age groups.[170]

Fifth, the straight-forward investment of public funds via the Homes and Communities Agency and the Greater London Authority to the housing associations can translate very directly into new Extra Care accommodation – fully equipped retirement apartments in a setting that can provide a full care service if needed, with dining facilities and opportunities for a full social life that banishes loneliness.[171] These developments are often seen as primarily meeting the need for care rather than for housing, in effect replacing the unpopular model of the residential Care Home.[172] But they also serve those

[168] The All Party Parliamentary Group for Housing and Care for Older People (2014),, *The Affordability of Retirement Housing,* p.7. http://www.demos.co.uk/files/Demos_APPG_REPORT.pdf?1415895320
[169] The All Party Parliamentary Group for Housing and Care for Older People (2014), *The Affordability of Retirement Housing*, p.28-29. http://www.demos.co.uk/files/Demos_APPG_REPORT.pdf?1415895320
[170] Lyons, M. (2014), The Lyons Housing Review. *Mobilising across the nation to build the homes our children need*, p.136. http://www.yourbritain.org.uk/uploads/editor/files/The_Lyons_Housing_Review_2.pdf
[171] Housing Lin, (2014) *The benefits of extra care housing on the quality of life of residents: The impact of living in Campbell Place, Fleet*. http://www.housinglin.org.uk/_library/Resources/Housing/Practice_examples/Housing_LIN_case_studies/HLIN_CaseStudy93_CampbellPlace.pdf
Aston Research Centre for Health Ageing (ARCHA) and the ExtraCare Charitable Trust, *A Longitudinal evaluation of the ExtraCare Approach,* http://www.aston.ac.uk/EasySiteWeb/GatewayLink.aspx?alId=245545
[172] Garwood, S, Joseph Rowntree Foundation (2013), *Older People with high support needs in housing*

with less pressing requirements and are shown to prevent care and health needs becoming more acute; they represent a successful blend of housing and care that can demonstrate impressive value for money.

## In conclusion

In conclusion, with very evident market failure in producing the homes this country needs, the challenge of housing our ageing population also represents a huge opportunity to support younger households. The State has a key role in creating the conditions for a very significant growth in house-building for those in their extended middle age, leading to considerable savings to the nation in health and care costs. It just needs enlightened politicians to recognise the potential and get behind the modest measures that could transform the housing position for old and young alike.

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*with care* p.11. https://www.jrf.org.uk/file/43753/download?token=zyalZ4EK&filetype=summary
Bazalgette, L. and Salter, J. Demos, (2013) *The Hanover @ 50 debate: Sociable housing in later life* http://homeshare.org/wp-content/uploads/2012/04/Sociable-Housing-in-Later-Life-May13.pdf

# In defence of the welfare state and the role of active housing policy

Danny Dorling, Halford Mackinder Professor of Geography, School of Geography and the Environment, University of Oxford

The UK welfare state is under attack. Those attacking it vehemently hate the idea of collective responsibility and have grown up with a particular belief, almost religious, that only markets are efficient. This group will age and disappear in time. Those who are younger than them have a very different experience of growing up, paying extortionate rents, being exploited by the market rather than fantasying about how good it could be. The young of the UK have been taught about market failure the hard way. That younger generation may well be the salvation of the welfare state as regards housing. They may bring in the rent regulation that the private sector so badly needs. But, before they become middle aged and are able to do this, there will be a battle.

It is easy to forget whom the welfare state should be for and what it should provide. The word welfare has been tarnished to the point that it is now equated with scrounger and malingerer. Benefits are now talked about as charity rather than as a right.

The welfare state is for all of us, but it does need to change. All of us can find ourselves suddenly in need. We can all fall ill, find that our loved one no longer loves us, or that our employer does not want us anymore. Even the incredibly economically successful need a welfare state. They need it not only to live in a society they need not be afraid of, but because (no matter how hard they try to hoard their wealth) some of their great-grandchildren or great nieces and nephews will come to rely on it. No rich family in history has ever managed to protect all its progeny for long. You can spend as much as you like on your children's education, but that will not secure their grandchildren's futures.

The welfare state is required for those goods that are too large, complex or rarely purchased for individuals to become experts in. No amount of information and transparency is a substitute for actual market experience. It is when you

learn from your many mistakes that the market works. We learn how to operate in markets from buying the wrong clothes, eating out in the wrong places, and listening to the wrong music. However, in cases of rare purchases you are usually a dupe and you need help because you do not know what you are doing. Children only have one shot at an education; none of us should want to learn from our mistakes by choosing the wrong heart surgeon. It is also not enjoyable to make the wrong choices in housing - we don't want to move home so frequently that we become experts at it. In all these areas there are sharks that will try to exploit the ignorant (and to a certain extent we are all ignorant) for profit. The welfare state protects us from the greedy and delivers goods and services that are accessible to all.

Fair future delivery models for health and social care, for pensions, for welfare, for housing and education should be based on those that are most successful in other countries with a welfare state. Unfortunately, (for us) our record is now very poor in all these areas, but should tell us we need to search for better alternatives to how we have allowed our welfare state to corrode. Consider for instance, our pensioners who are destined to mostly subsist in poverty if they live long enough. The Table below shows the most recent median incomes of better-off tax paying pensioners in London. An income of £11,000 a year (in Hackney) is £30 a day. Our elite are so ignorant of the simplest social statistics that they have no idea that the average tax paying pensioner, including those pensioners living just a few miles from the Houses of Parliament, survive on so little.

## Income and tax by borough and district or unitary authority, 2012-13 (taxe payer only)

| County and district / unitary authority | Self-employment income | | | Employment income | | | Pension income | | |
|---|---|---|---|---|---|---|---|---|---|
| | n | Mean | Median | n | Mean | Median | n | Mean | Median |
| **London** | 568 | 31,000 | 12,200 | 3,140 | 36,800 | 24,000 | 663 | 16,800 | 13,300 |
| **Barking and Dagenham** | 10 | 15,300 | 14,200 | 60 | 23,500 | 20,700 | 11 | 11,200 | 11,700 |
| **Barnet** | 31 | 29,400 | 12,700 | 129 | 35,500 | 23,000 | 37 | 17,100 | 13,300 |
| **Bexley** | 13 | 16,100 | 12,700 | 85 | 28,500 | 23,500 | 31 | 14,900 | 13,400 |
| **Brent** | 23 | 18,300 | 11,600 | 116 | 26,200 | 19,900 | 19 | 12,800 | 11,200 |
| **Bromley** | 23 | 23,700 | 13,500 | 122 | 35,400 | 26,200 | 48 | 19,100 | 15,600 |
| **Camden** | 18 | 87,800 | 14,500 | 85 | 55,800 | 27,900 | 15 | 22,400 | 14,100 |
| **City of London** | 2 | 144,000 | 81,400 | 7 | 116,000 | 55,100 | 1 | 26,400 | 15,000 |
| **Croydon** | 21 | 18,100 | 10,800 | 133 | 29,700 | 24,000 | 41 | 16,800 | 14,800 |
| **Ealing** | 25 | 20,700 | 11,700 | 129 | 31,000 | 22,600 | 25 | 15,100 | 12,700 |
| **Enfield** | 19 | 22,200 | 12,500 | 110 | 28,400 | 22,400 | 30 | 15,200 | 12,800 |
| **Greenwich** | 16 | 18,500 | 11,200 | 93 | 30,400 | 22,900 | 19 | 15,200 | 13,000 |
| **Hackney** | 18 | 22,500 | 11,100 | 84 | 30,300 | 24,100 | 9 | 12,200 | 11,000 |
| **Hammersmith and Fulhai** | 12 | 41,100 | 11,700 | 78 | 49,400 | 25,700 | 11 | 18,700 | 13,100 |
| **Haringey** | 23 | 25,500 | 11,600 | 97 | 32,400 | 22,400 | 16 | 17,300 | 13,200 |
| **Harrow** | 20 | 22,900 | 12,600 | 94 | 29,800 | 22,400 | 26 | 15,700 | 12,500 |
| **Havering** | 17 | 20,500 | 14,700 | 91 | 30,600 | 24,500 | 36 | 15,100 | 13,900 |
| **Hillingdon** | 16 | 18,300 | 12,400 | 106 | 29,000 | 23,000 | 29 | 15,900 | 13,400 |
| **Hounslow** | 17 | 24,900 | 11,700 | 109 | 30,300 | 22,100 | 20 | 13,100 | 11,600 |
| **Islington** | 15 | 45,000 | 13,400 | 90 | 43,200 | 27,200 | 11 | 18,100 | 12,400 |
| **Kensington and Chelsea** | 12 | 122,000 | 12,500 | 55 | 113,000 | 34,000 | 12 | 26,000 | 12,500 |
| **Kingston-upon-Thames** | 11 | 27,800 | 12,000 | 65 | 38,000 | 26,300 | 18 | 17,600 | 14,300 |
| **Lambeth** | 19 | 23,800 | 11,700 | 130 | 35,400 | 25,400 | 13 | 15,400 | 12,300 |
| **Lewisham** | 17 | 16,600 | 11,100 | 100 | 29,600 | 23,100 | 18 | 14,700 | 13,200 |
| **Merton** | 14 | 44,400 | 11,600 | 84 | 39,500 | 25,200 | 18 | 17,400 | 13,400 |
| **Newham** | 20 | 13,700 | 11,500 | 108 | 23,000 | 18,800 | 9 | 12,800 | 11,500 |
| **Redbridge** | 19 | 20,100 | 13,100 | 97 | 30,500 | 23,900 | 26 | 15,800 | 13,200 |
| **Richmond-upon-Thames** | 15 | 39,800 | 12,200 | 78 | 54,800 | 30,900 | 25 | 20,900 | 15,400 |
| **Southwark** | 17 | 27,200 | 10,900 | 117 | 35,000 | 24,300 | 13 | 15,900 | 12,500 |
| **Sutton** | 13 | 18,500 | 12,500 | 74 | 30,700 | 25,200 | 21 | 16,900 | 15,400 |
| **Tower Hamlets** | 12 | 20,900 | 11,100 | 104 | 37,600 | 24,500 | 7 | 16,600 | 12,200 |
| **Waltham Forest** | 23 | 15,100 | 12,500 | 93 | 26,000 | 21,900 | 16 | 14,800 | 14,100 |
| **Wandsworth** | 20 | 48,400 | 12,500 | 131 | 49,600 | 29,200 | 20 | 18,300 | 13,300 |
| **Westminste** | 14 | 106,000 | 14,200 | 82 | 75,900 | 29,800 | 14 | 29,600 | 15,000 |

Source – HM Revenue and customs, Nation Statistics (approved by ONS) last updated March 2016: "National Statistics: Income and tax by borough and district or unitary authority, confidence intervals"[173]

## Taking action: How can we solve the housing challenge to support equality?

We look long-term. If we look to the United Provinces (the richest place on Earth before the United Kingdom became so rich) at their heart, in Amsterdam in 1699, a house sold for 28,100 guilders. This was a very fine house. Its

[173] https://www.gov.uk/government/statistics/income-and-tax-by-borough-and-district-or-unitary-authority-confidence-intervals

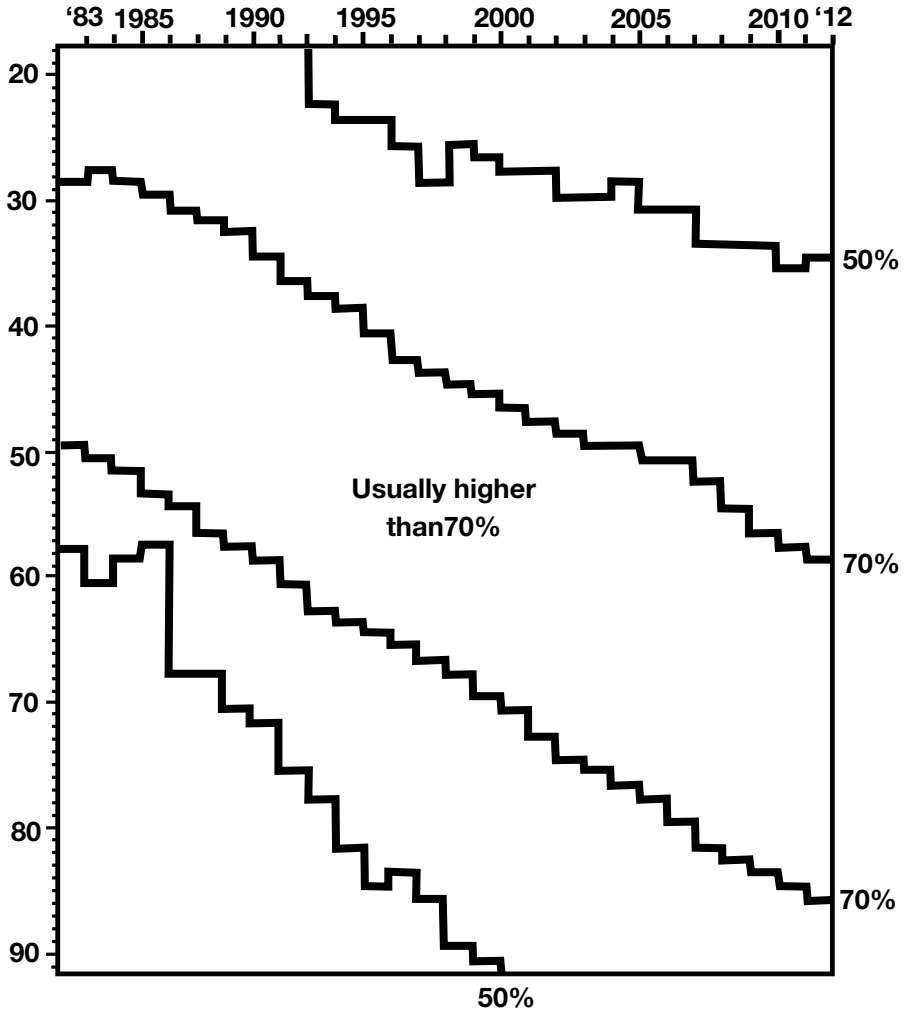
equivalent would be found in Kensington today. The house in question was number 20 Herengracht, on a street that was situated on the most sought after canal in the city. That sale represented a real terms rise of 15% on its 1669 sale price. It was valued then, in today's money, at just under half a million Euros. The world as a whole was far poorer then so this was a true fortune. The value of the house rose again to peak in 1738. For seven decades' prices had risen and risen. The Dutch elite must have believed they could never fall.

Prices on Herengracht fell by a third to 1751, and then as Neil Monnery, who documents all this puts it succinctly, they fell again and again : "prices would reach their 1740s levels once more in 1778 and then not again for 250 years"[174] You could look more recently at Tokyo in 1990, or at Dublin in 2008, or all around the world but London. A 1980s degree from Oxford in modern history doesn't teach you stories such as this. George Osborne may well still not be aware of the possibilities. We all need the welfare state not only because none of us can foresee what might happen to us individually, but because markets (and especially housing markets) are unpredictable and stability is far from common.

Figure 1 is a simplified version of a much more complicated graph first published in the Telegraph Newspaper. In the figure, each cell represents people of a particular age and the numbers outside those cells represent the proportion of that age group at that time who were homeowners (i.e. buying a home with a mortgage or owned it outright). Housing has become unaffordable, which is why the lines slope down to the right. But that does not mean that most people will now rent forever. It means that house prices are now unsustainably high. By 2012, more than 50% of people in their twenties and early thirties were renting representing a dramatic change from only a decade ago when most lived in mortgagor households. If the trends shown in Figure 1 continue, then in ten years' time a majority of people in their forties will be renting privately, and in another ten years, a majority in their fifties will be. This is why Figure 1 is so important – it shows us where we are currently heading.

[174] Monnery, N. (2011) Safe as house? A Historical Analysis of Property Prices, London: London Publishing Partnership. Pages. 84-85.

**People with a mortgage or who own outright in the UK by age 1983-2012 (% within single year of age and year group)**




Note: Data missing for 1988 and 1992, the trends have been interpolated over those years

Source: Analysis by the author of the British Social Attitudes Surveys

So what can we do? The answer is an enormous amount. A renewed welfare state could incorporate private renting but control it. The standard length of private rented tenure in the UK should be lengthened to three years, or five

years for people with, or who subsequently have, children. Rents must not be increased during this period, since people should not be losing more than a third of their disposal income in rent; a huge number of recent reports and studies make this claim and cite an enormous amount of data in support of it.[175] Social housing rents should be subject to regulation, to ensure that they are not excessive: again, not more than 30% of disposable income. Tenants who might wish to leave their tenancy early could still do so, but landlords could not insist that they do. If the quality of accommodation is substandard, tenants should have the right to improve it, deduct the cost from their rent, and extend their tenancies by more years in proportion to how much they had to spend. That would give the landlord an incentive to ensure the accommodation was up to standard. It would also ensure our housing stock was improved. If you think this is impossible consider how the right to roam was introduced. The land in England is still owned by the landowner, but we all have a right to roam over it and they have a duty to keep the paths clear and the styles well repaired. Lives can be improved by improving rights without the need to nationalise land or housing.

## Under-occupancy

Housing is in short supply because it is now being used in Britain in a way that is more inefficient than at any time since good census records of our use of housing began in 1911. A higher proportion of homes are empty or more rooms in them are under-used than ever before. Almost all of this inefficiency is in the private sector and mostly found among those who own outright. It is largely due to older homeowners holding on to large properties that are too big for them, but they keep them for the rising asset value, possibly hoping to pass that on to their children when they die – to try to protect their children.

Annual wealth (including housing wealth) taxation is needed because the alternative is that a small group becomes ever wealthier to the detriment of the rest, or that we stoke up the size of the eventual crash to be from even dizzier heights. Progressive property taxation would achieve a great deal, as could a flat tax on the value of property owned or proportional to total land value.

[175] See the final report of the London Fairness Commission of 2016: http://londonfairnesscommission.co.uk/

## Building more homes

We have to build because our population is rising and we are lucky that it is. We have to build retirement apartments with lifts near to where we currently live that are attractive enough for people to occupy by downsizing to. I am writing this chapter from the 17th floor of a tower block in the middle of the city in Berne in Switzerland. The tower-block has wonderful views of the city and the mountains around it. It is located by the main railway station and by the medical institute where I am working today. All the residents on the floors below me are very old. Proposals that may appear impossible in England have long ago been implemented elsewhere in Europe.

We have to build homes in and near cities where people will not need more cars to use those homes. And we have to ensure that the value of housing begins to fall towards normal European levels so that there is a disincentive to horde. The purchase of housing to leave empty as an investment should be made unaffordable by increasing taxation on empty homes and ensuring that capital gains tax applies to all property. We also need decent pensions so people don't bet on housing for their retirement income.

## Rent regulation

In the Netherlands tenancies are regulated; the quality of rented housing is higher; price is lower. In France, rented homes are much more spacious, on average, than in the UK. In the US, property taxes are fairer. In Japan they are decades ahead of us in terms of planning housing to fit public transport, so for decades' car use there has been falling.

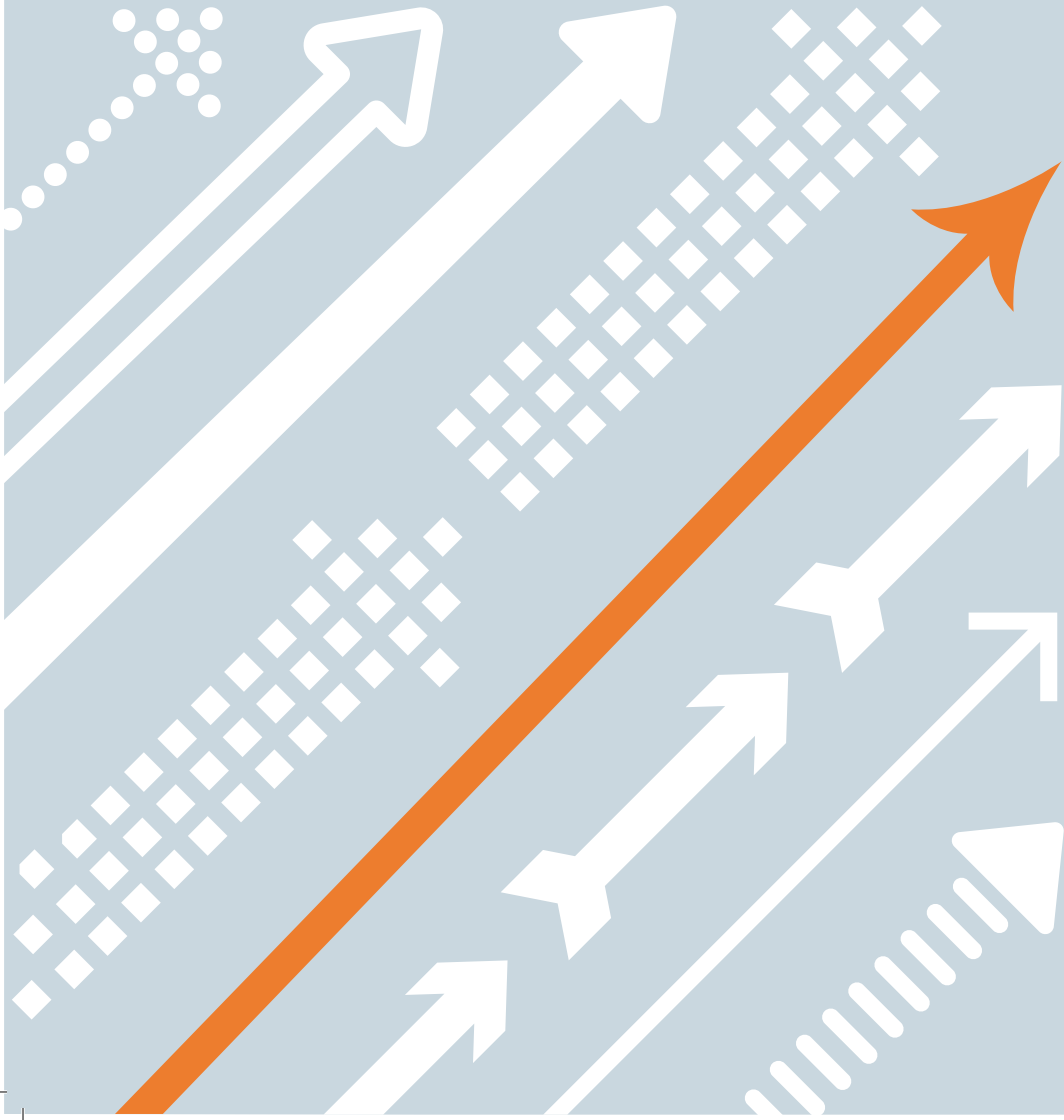
Housing in the UK needs to be for homes again, not for investment and speculation. We need to look abroad to see how to do this. We need to look at how housing policy in other countries has also contributed to better mental health in those countries. Of course, there is much more to do than this. For instance, the Swiss choose to dedicate twice as much, per head, on health spending compared to the British – but that is not the only reason why they are healthier. Nowhere is perfect, but so many places are so much better than we are in the UK. The entire continent of Europe now provides examples of many different variant of the welfare state. Although the UK was the first country in Europe to adopt this model we have forgotten how valuable it is and have become complacent. The same has happened in New Zealand that introduced

a welfare state before us. The future will not be a re-run of the past. All good ideas are adaptations of ideas at least partly tried out first somewhere else. So let's look out and learn from our immediate geographical neighbours. To see what would happen to us if we do not just consider how so many people are so insecurely and poorly housed in the USA[176]. There is no need for us to be so stupid in future.

In conclusion, large and difficult changes will need to be made if we are to sustain and renew the welfare state in future: educate all children well, house everyone well, maintain a decent health service and good employment prospects for all, as well as good pensions.

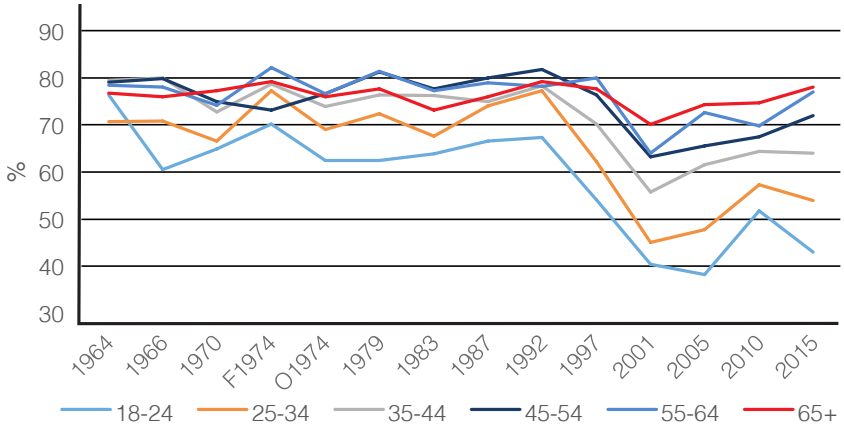
[176] Dorling, D. (2016) Evicted: Poverty and Profit in the American City, by Matthew Desmond, The Times Higher, March 3rd: https://www.timeshighereducation.com/books/review-evicted-poverty-and-profit-in-the-american-city-matthew-desmond-allen-lane

# **Part 4.** Building a consensus on the way forward



# The political landscape

## Election turnout by age

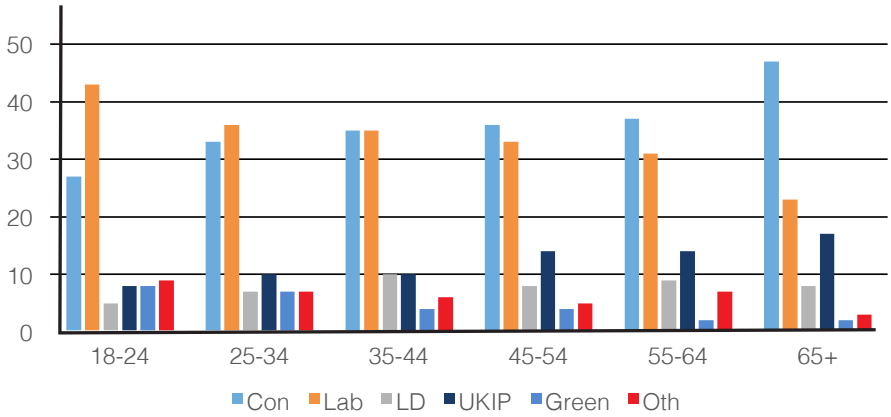



Source: We have combined the results from the British Election Study (1964-2010) with Ipsos MORI polling results for 2015 General Election

**In 2010,** only **51.8% of voters** aged between **18-24 voted** compared to **74.7% of people over the age of 65.**

**In the 2015 General Election**, only **43% of 18-24 year olds voted**, compared with **78% of people aged over 65.**

## Voting by age group, UK General Election 2015




Source: Ipsos MORI

**At the last General Election, approximately 47% of people over the age of 65 voted Conservative**, while **23% voted for Labour** and **17% voted for UKIP.**

**In contrast**, of people aged between **18-24, only 27% voted for the Conservatives**, while **43% voted for Labour.**

# Overcoming political short-termism: How can we deliver a new long term social contract in the context of population ageing?

Nusrat Ghani, Chair of the All-Party Parliamentary Group on Ageing and Older People, and Member of Parliament for Wealden

What do we expect from the state? Have our expectations become overzealous? Do we demand more than we deliver? Do we get less than we should expect? Are we wrong to focus on the relationship between the individual and the state in isolation?

Today, nobody would really give much credence to arguments against the delivery of social policy in developed countries, and rarely does a serious politician even mention opening up a major discussion about a restructuring of the welfare state. Yet, despite this level of consensus, there remains huge disagreement over what it is social policy is there to achieve and what the optimum approach towards the role of the state should be. These disagreements are not the ones which define the cut and thrust of day-to-day political discourse, even though they should be.

To start from first principles, I have always found it interesting that those who advocate a large and interventionist state all too often defer to William Beveridge to defend their ideal. Beveridge, whose approach was of course most famously set out in his 1942 report, set out the foundations of some the welfare state's key pillars. Yet from his writing it is clear that he favoured a set of social policies whose central goal was to provide a basic level of welfare, in order to provide a safety net and prevent the exploitation of the vulnerable. His five giants – want, squalor, disease, ignorance and idleness – were seen as social evils which none should have to contend with; his solution to those evils, made reality through the post-war welfare reforms, was the basic level of individual welfare required for them to be tackled and to support the individual back onto their feet.

Beveridge was not the first to seek to protect the poor, since the Fabian Society had been campaigning for the introduction of social protection through the

state from the 1880s, partially in reaction to the poverty surveys of Booth and Rowntree at around the same time, which showed levels of poverty to be far higher than had previously been assumed. But Beveridge's preference was to establish a welfare state which allocated resources on a minimal, needs-based basis. He wrote in 1942 that 'The State in organising security should not stifle incentive, opportunity, responsibility; in establishing a national minimum, it should leave room and encouragement for voluntary action by each individual to provide more than that minimum for himself and his family'.[177]

In the context of population ageing, the role of the state in our lives from birth to death is put into stark focus. How does the state bear the burden of a longer lifecycle? How does it do so fairly, between different generations at one moment in time, and the same generations at different points in time? How does it do so sustainably, if population ageing is to continue over time? And perhaps one of the answers is that to embark on a smart examination of the challenges faced, and a realistic consideration of where provision is most suitable, can see current standards maintained.

As an MP, I am very aware of the demographic changes facing our country. My constituency of Wealden is located in East Sussex, which has the highest number of over-85 year olds in the country. One in four of the population is aged 65 and over. I am proud to be Chair of the All-Party Group on Ageing and Older People, as well as a dementia friend. Dementia is just one of the challenges we face as a country in the context of an ageing population – how can we as a county in East Sussex, given that as many as one in three people aged over 65 may develop dementia, respond to dementia with effective health and social care in the context of a reducing pool of taxpayers?

Short-termism in politics is never going to be overcome. All of us, in our nature, have difficulty thinking long-term. Not just because of the uncertainty which by definition accompanies long-term planning, but because we naturally place a lower value on the future than we do on the present. We know we can benefit from something now, so why would we delay that benefit to the future if we cannot be as sure that we will be in a position to benefit from it then. Why risk rejecting something today which we might not be in a position to accept tomorrow?

And so it is in politics. But for the sake of society, and the prosperity and security of future generations, we have a responsibility to start the conversation.

[177] Beveridge, W. (1942), The 1942 report on Social Insurance and Allied Services, November

It is easy, and a cliché, to call for a national conversation about something. Usually it is a way of postponing difficult decisions and giving the illusion of listening to the public, rather than being accused of just making decisions. But a national, and honest, conversation is the least we should demand. The welfare state cannot continue in its current form forever. It is unsustainable and unrealistic, and we are being dishonest if we claim otherwise. The NHS, to focus on just one area, is financed on a pay-as-you-go basis from a societal point of view – it does not have the capacity or flexibility to be an insurance system with reserves put in place to pay for the potential health and care needs of today's young people when they reach old age, and the health and care difficulties that naturally result. If we truly love the NHS, we have to make it workable for those future generations.

One of the key hurdles to overcome is to reject the scaremongering of those who respond to any suggestion of tinkering with state structures by saying that those most in need will suddenly be left helpless, or that the NHS will suddenly stop saving lives. Reforming the welfare state so that it becomes sustainable does not mean compromising the core values of the welfare state. Indeed, only with reform will we be able to achieve the desired outcomes of Beveridge and Bevan in the future.

A feature of social policy that Beveridge did not touch on to such a great extent was its relationship with citizenship, and the benefits that social policy can bring to society as a collective entity rather than to each individual on their own. T.H. Marshall wrote of the progression of citizenship over time, dividing it into the possession of civil rights and individual freedom, then the exercise of political power through participation and voting and, finally, a feeling of social independence. He cites the right to economic welfare as a key part of being a citizen and says that an individual is not a citizen without the ability to 'share to the full in the social heritage and to live the life of a civilized being according to the standards prevailing in the society'.[178] The latter is a nod towards requiring a certain standard of welfare and thus the state's duty to provide such a standard. However, included in this is also a duty on the part of the individual to play his or her part in making society as a whole better, rather than just working for his own ends.

And perhaps one focus of the conversation should be on a change to the relationship between the state and the individual. Should we refocus the social

[178] Marshall, T.H. (2006), 'Citizenship and Social Class', in Pierson, C. and Castles, F.G. (eds.), The Welfare State Reader, Polity Press, p.30

contract to fit today's Britain? Would a new contract, between the individual and society, with the state as a third party, be a more sustainable reflection of modern-day realities?

I am as keen as anyone to delve into the detail of how we adapt the state to the needs of modern society – how, for example, do we better facilitate an individual or a couple's use of their pension to fund their social care? How do we make it easier for one person to use their own pension to fund their partner's social care? How do we encourage first-time workers to think immediately about their pension by, for example, highlighting on their first payslip the contribution they are making, or not making, to their pension, and pointing the way to advice on thinking long-term? Life is a ticking clock, and we need to be checking the time well before retirement.

But before we consider these questions, we have to engage in a wider discussion about the issues in which those questions are wrapped up – how do we link health and social care? How do we reassess expectations? How do we encourage greater long-term thinking on the part of the individual, as well as the politician?

Reaching a consensus will not be easy. but one of many starting points for the conversation should be the importance of investing in children and young people, and giving young people the tools to save for a pension of their own. The current government is already doing that, with its focus on academies and its introduction of measures such as the Lifetime ISA. Through these measures, we can yield an individual and social dividend in the future by enhancing the skills available to individuals from their youth to their dotage, and diminishing the risks of old-age poverty. Without truly joined-up policymaking across government, however, we will struggle to achieve what we wish to achieve.

Another starting point should be the role of the mixed economy. If we were to refocus the social contract from one between the individual and the state to one between the individual and society, the mixed economy becomes even more important. How do we shift the consensus to one that accepts that the state is not the only source of security or support? How can the private and public sectors both work together with families and with communities to build a society in which the state is just one cog, not the whole machinery?

My journey to representing Wealden in Westminster started with an experience of politics much like many of those who end up in this career – far from positive. When I questioned self-appointed local leaders and union activists about their

low expectations of me, and their presumption that opportunities for someone from my background would be limited, they responded with little more encouragement than that the state would always be there to manage me, and make decisions about my life's course.

Not only do I have a problem with such a lack of aspiration and belief, but our demographic changes also make it increasingly unrealistic and unfair to provide a false prospectus to today's young people that the state can continue to offer the same type of support structure that it has done since the war.

So how do we get this national conversation going, and ensure that it is an honest one with all cards on the table? At the time of writing, I am fortunate to have completed ten months as a Member of Parliament. Lots of things have surprised me during those months, but one of the most surprising has been seeing friendly collaboration between MPs of different parties on issues of importance for communities and society as a whole. This is one such issue.

The House of Lords led the way a few years ago with its cross-party Committee on Public Service and Demographic Change, which concluded that Britain was "woefully under-prepared" to deal with the challenges of an ageing society.[179] But we cannot deal with those challenges, and get answers, without asking the right questions.

Those questions have been parked to one side because they are difficult and because they hint at change. But as a society, how have we allowed ourselves to get to the stage where, for example, a significant proportion of the working population simply do not think about the income they will receive once they retire? Culturally, we have become obsessed with making sure we have the right salary for the job we have, but we are not obsessed with working out how much of that salary should be set aside for our "salary" once working life is behind us, when that phase of our lives is another twenty to forty years ahead of us.

We need a renewed attempt to bring together politicians, academics, commentators, health and social care workers, pension experts and others to frame the questions that society must answer: what do we expect from the state? Have our expectations become overzealous? Do we demand more than we deliver? Do we get less than we should expect? Are we wrong to focus on the relationship between the individual and the state in isolation?

[179] House of Lords Select Committee on Public Service and Demographic Change, Report of Session 2012–13: Ready for Ageing? (p.7)

To get answers, you need questions, so let's decide what they are and ask them. Only then can we begin the conversation we so desperately need in order to secure a sustainable, fair and honest social contract for the future.

# Conclusion: Towards some principles for reform

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***"…any proposals for the future, while they should use to the full the experience gathered in the past, should not be restricted by consideration of sectional interests established in the obtaining of that experience. Now, when the war is abolishing landmarks of every kind, is the opportunity for using experience in a clear field. A revolutionary moment in the world's history is a time for revolutions, not for patching."***

Sir William Beveridge 1942

## Introduction

This volume has sought to bring together a group of experts from many different fields in order to consider how the welfare state should respond to the challenge of population ageing. But making proposals and arguments is one thing, taking action is another. Implementing reforms of any kind is a tough business, especially if what is proposed is likely to have far reaching distributional impacts for different groups. In this context, we conclude the volume by asking, is reform possible, and if so, how can we ensure that reforms are well designed and capable of securing political support?

## Is reform politically possible?

Reforming the welfare state is going to be a challenge. It is likely to necessitate cutting back on spending in some areas while expanding others. But reducing aspects of state expenditure is not easy – there are strong vested interests that deter and prevent such efforts. Pierson's influential article from the mid-1990s argued that despite increasing concern about the crisis of the welfare state and the rise of neo-conservatism in the UK and the United States in the 1980s, the welfare state remained well and truly intact[180]. Others have disagreed with this view and argued that, on the basis of better measures of retrenchment, those same governments managed to reduce the size of the state[181]. Recent events in Europe also show that governments are able to pull back the welfare state.

[180] Pierson (1996) The New Politics of the Welfare state: *World Politics* 48 (January 1996), 143-79
[181] Allan and Scruggs (2004) Political Partisanship and Welfare State Reform in Advanced Industrial Societies, *American Journal of Political Science*, Vol. 48, No. 3, July 2004, Pp. 496–512

But many agree that retrenchment is often unpopular and can have significant political costs for incumbent governments.

While the politics of retrenchment are complex, there are a number of emerging themes within the literature on what systems, conditions and strategies are most conducive to reform efforts.

1. **Strong majority governments.** Governments with large majorities are more able to weather the unpopularity of reform and therefore better able to implement them.

2. **Lacking in veto players.** The system of government matters. Broad coalition governments are likely to find it harder to pass laws and make significant reforms than single party majority governments where there are fewer individuals and interest groups to veto proposed reforms.

3. **Budgetary crises provide a "burning platform".** As we have seen across Europe since the financial crisis, governments can use budgetary crises as justification for reform efforts. Similarly, years of economic stagnation might be seen as a credible reason for proposing wide-spread reform.

4. **Communication vs obfuscation.** While it is often argued that introducing reforms by stealth is a good tactic to avoid public backlash, recent research suggests that in fact clear communication of reforms is the better approach since it leaves governments less vulnerable to opposition attacks[182].

5. **Claiming credit for reform can be a vote winner.** Reform, including retrenchment does not have to be unpopular. Indeed, it has been suggested that political parties can, under certain conditions, actually gain votes by claiming credit for austerity policies[183].

6. **There is no alternative.** Bold retrenchment policies have been justified by the Italian and Spanish governments through a "´there is no alternative´ strategy", which, according to some, creates limited interaction space between social and political actors.

[182] Elmelund-Præstekæra, Klitgaarda and Schumachera (2015) What wins public support? Communicating or obfuscating welfare state retrenchment, *European Political Science Review* / Volume 7 / Issue 03 / August 2015, pp 427-450

[183] Giger and Nelson (2010) The electoral consequences of welfare state retrenchment: Blame avoidance or credit claiming in the era of permanent austerity? *European Journal of Political Research* Volume 50, Issue 1, pages 1–23, January 2011

### Where does the UK sit on this spectrum?

With a first-past-the-post electoral system which often, though not always, generates, majority governments, the UK's political system ticks a number of boxes making it more conducive to retrenchment than most. But while the UK's system might be well suited for implementing wide-reaching reforms, this is not the same thing as implementing sound and good reforms. Indeed, in Professor King and Crewe's seminal book, the Blunders of our Governments, it is argued that UK governments of all political persuasions have been prone to monumental cock-ups. The authors identify a number of underlying causes of blunders including (amongst others): a weak parliament, departments and ministers working in silos, ministers who have little prior experience in their policy area and who are frequently shuffled around, and a deficiency of deliberation due to the regular presence of elected majority governments[184]. As the authors note:

*"The British system lacks – and is widely thought to benefit from lacking – a significant number of what are sometimes called veto players: individuals and institutions whose backing is needed for the taking of any major initiative…The only trouble with a system in which it is easy to take decisions is that it is every bit as easy to take the wrong decisions as it is to take the right ones".*

Therefore, decisiveness of action, which is a particularly prominent feature of the UK's political system, may be both a strength as well as a weakness. The UK may be better placed to make wide-reaching reforms, but the risks of getting it wrong remain strong.

### How can we move forward?

Reform of the welfare state to ensure its future sustainability is not simply about pulling back the state. This volume has identified the importance of strategies to promote full employment and higher productivity, better integrated health, social care and community support to meet the rising demands of the elderly and more investment in education and housing to support the growth of human capital, housing affordability and social cohesion. A reconfiguration of the state is therefore likely to require retrenchment in some areas and expansion in others in order to meet the needs of our ageing population. But there will be winners and losers along the way, and governments will need to carefully consider how to manage these. The task is not insurmountable. An open and transparent national debate about the challenges posed by population ageing

[184] King and Crewe (2013), The Blunders of our Governments, A Oneworld Book.

and the possible implications for public policy would be a good start. But a debate is one thing, taking action is another. With the above in mind, we outline six key principles to kick-start a process for debating, analysing and ultimately implementing reforms to the welfare state in the context of population ageing:

1. **Define the problem:** To what extent should the problem be defined as one about the future sustainability of government spending, versus broader notions of material wellbeing and social cohesion. The issues are connected but may, in many respects, compete with one another. For instance, reducing public spending on pensions might improve the government's finances in the short run but would lead to ridicule if it resulted in a destitute elderly population.
2. **Understand the different dimensions of the problem:** We need to have a debate about the relative size of the various challenges informed by detailed empirical analyses. This might, for instance, include analyses of the likely impact of ageing on the economy (including productivity, employment and interest rates), how ageing will affect the demand for health and social care, income shortfalls in retirement and future housing needs (amongst others). Alternative scenarios should be developed in consultation with a broad, multidisciplinary team of experts.
3. **Identify a competing set of solutions/coping mechanisms**: There are likely to be many possible policy options in order to cope with the adverse impacts of ageing on the sustainability of government finances and the wellbeing of the population. A broad set of options for reform should be considered and their potential impacts on spending and wellbeing carefully modelled. Particular emphasis should be placed on understanding who are likely to be the winners and losers followed by an exploration of how to best support those who stand to lose out.
4. **Think holistically:** When considering options for reform, it is easy to compartmentalise potential impacts. But reforms in some areas such as housing or the labour market are likely to have far reaching implications on other areas such as pensions or health. It is therefore vitally important that the systemic impacts of reforms are carefully thought through.
5. **Use a wide variety of experts in the deliberation process but do not be constrained by special interest groups:** Consistent with the views of King and Crewe, in order to avoid constructing badly designed policy proposals, experts from a variety of different fields should be involved in

defining the problem, understanding it and devising potential solutions. As the authors themselves note "not deliberating is beyond any doubt a very bad idea". But critically, the ultimate decision for what policies are implemented do not rest with the group of experts consulted during the policy forming process, but explicitly with the government of the day. In this regard, government should not be constrained by special interest groups but by the relative merits of the reform options in relation to the challenges that have been identified.

6. **Communicate proposed reforms in a clear and transparent way:** The original Beveridge report was remarkable in many ways. But perhaps one aspect that deserves more attention is the effort which was taken to explain the proposed reforms, during a time of war, in a simple and understandable way. In this regard, while the underlying analyses of the challenges posed by population ageing and the potential options for reform may be complex, great attention must be taken to communicate the outputs and implications of such analyses in ways that are understandable for those with little or no prior knowledge of the issues. While this our last guiding principle, it is perhaps the most important.

We began this volume by arguing that population ageing, the welfare state and democracy might be incompatible. We provocatively argued that if governments make policy based purely to get re-elected, the welfare state could become so distorted that it might sow the seeds of its own demise. To move forward, we, as a society, need to understand the long-term consequences of such an arrangement. It is quite possible that by having an honest and open national debate about the possible economic and social consequences of ageing, public opinions could be reshaped and current political preferences challenged. It is certainly worth the risk. The time for a proper debate on the future of the state has come.

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