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@TheIFS

Patterns of spending in retirement



Economic
and Social
Research Council

Background and motivation

- In the past UK pension incomes were mostly fixed over time
- This has changed in recent years
 - Shift from defined benefit to defined contribution pensions
 - Pension freedoms have removed the effective requirement to annuitize
- People in the UK now have more flexibility in deciding their income profile in retirement
- Preferred spending patterns in retirement will affect how people should be thinking about drawing down their pension wealth

Research question

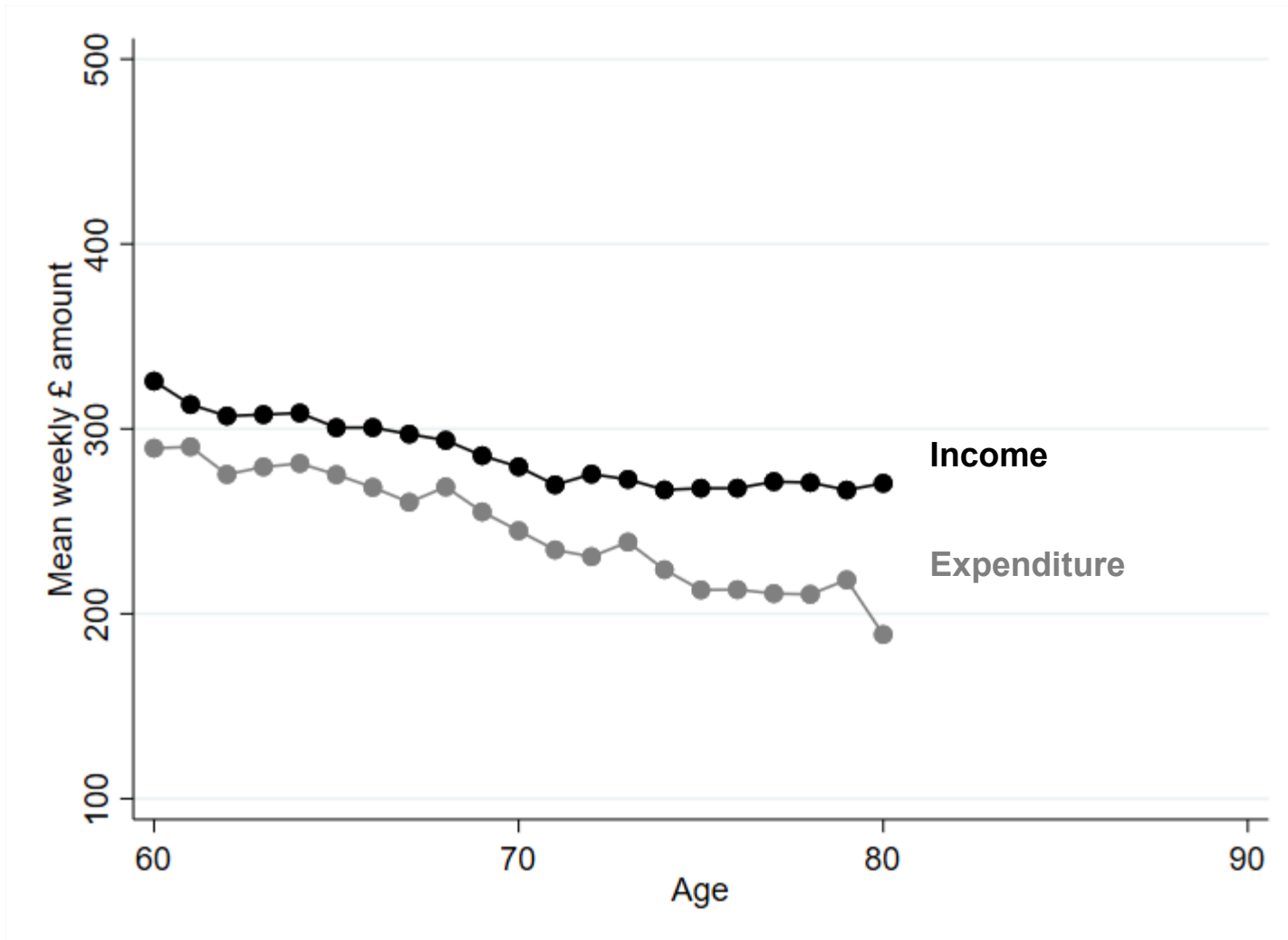
- How does spending change through retirement?
- Cross-sectional average spending by age suggests expenditure declining at older ages
- This might be misleading:
 - Cohort differences
 - Differential mortality

Dataset: LCFS



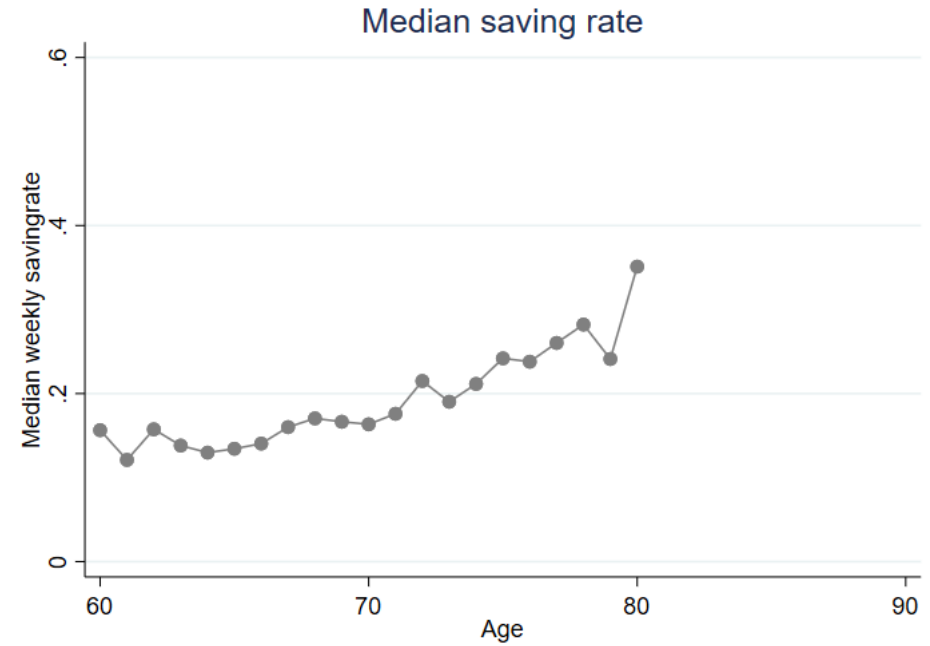
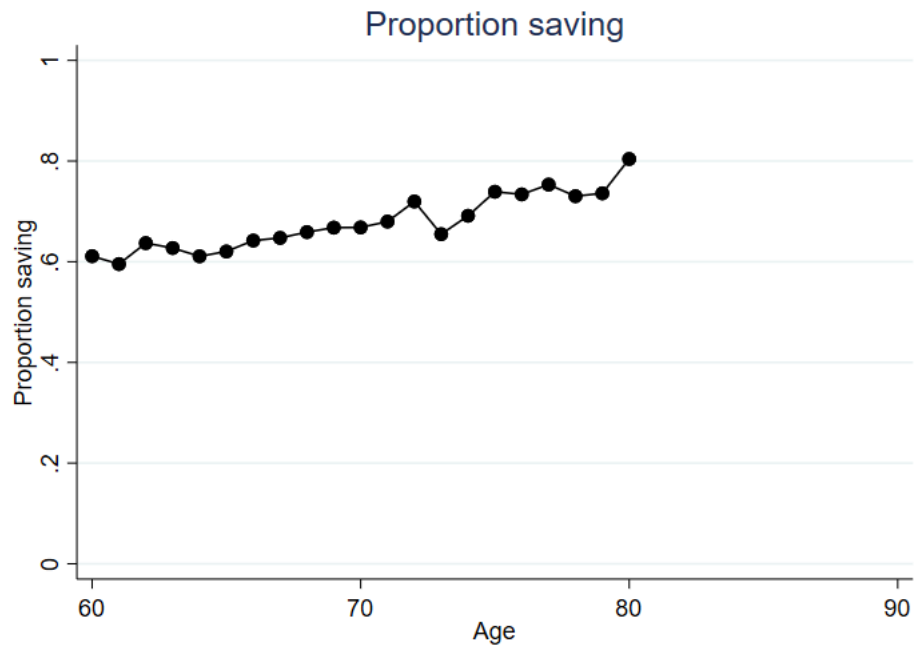
- Start by examining spending patterns using the Living Costs and Food Survey
 - Detailed information on all household expenditure
 - Key household and individual demographics
- We adjust expenditure and income for:
 - Inflation (all amounts are in real 2019 £ per week)
 - Household size, by dividing household level expenditure and income by number of people in the household
- Current analysis using data where age is top-coded at 80

Cross-sectional average spending and income



Notes: LCFS 2003 to 2016

Cross-sectional average saving

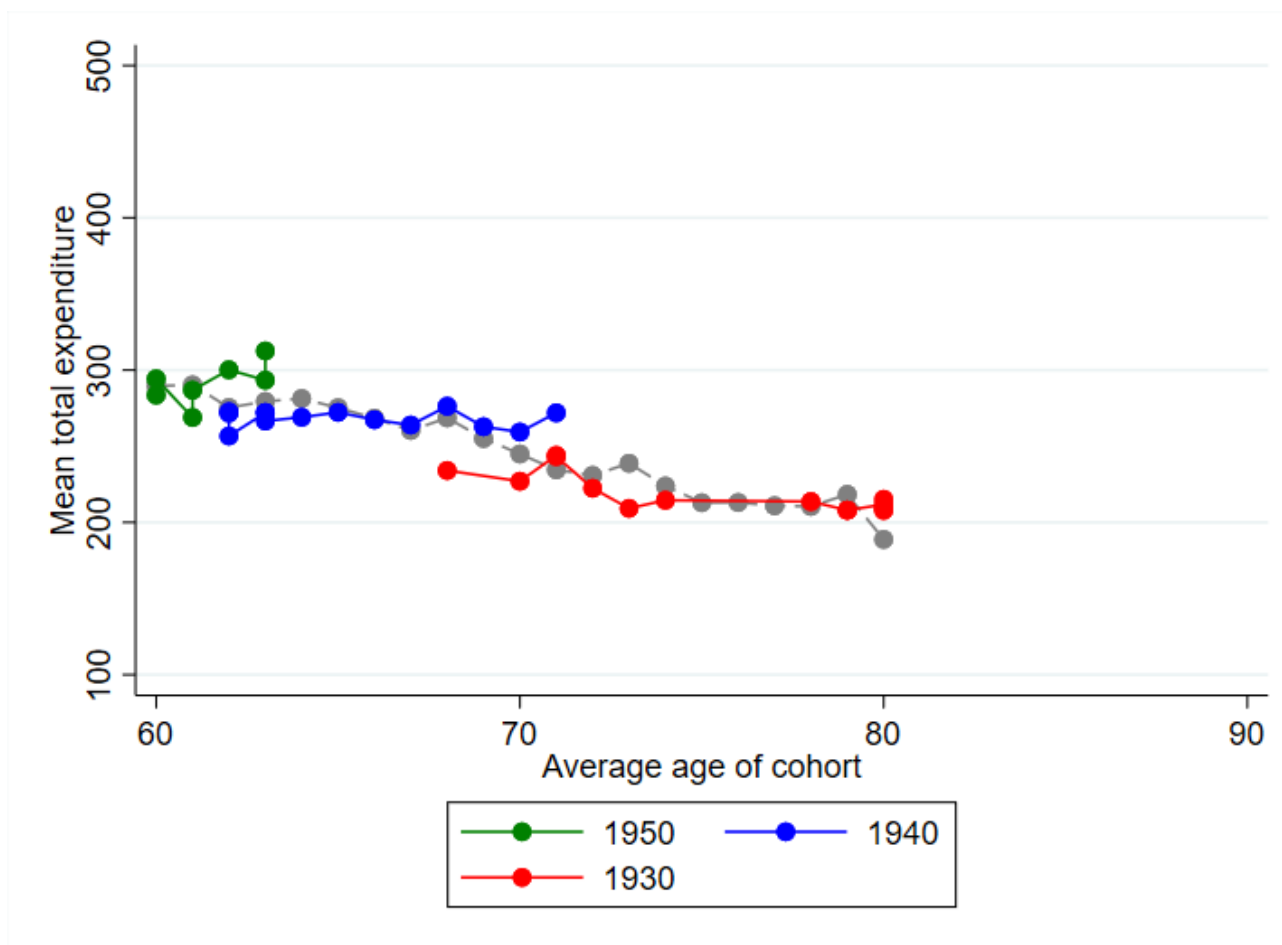


Notes: LCFS 2003 to 2016

Cohort differences

- Age profile does not give full picture
 - We know different cohorts have different earnings over their lifetimes and different resources in retirement
 - → Different cohorts may also have different levels of spending at the same age

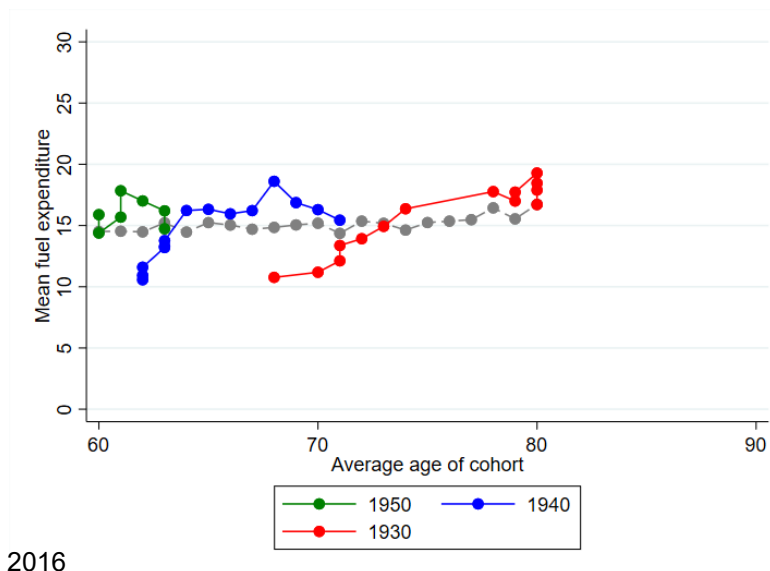
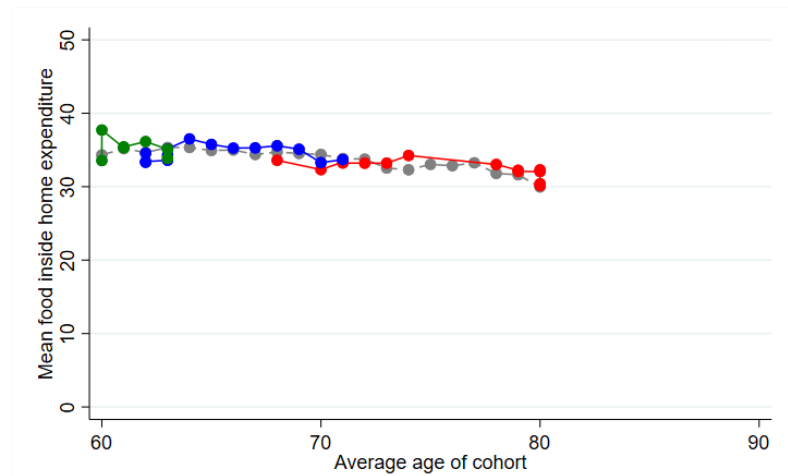
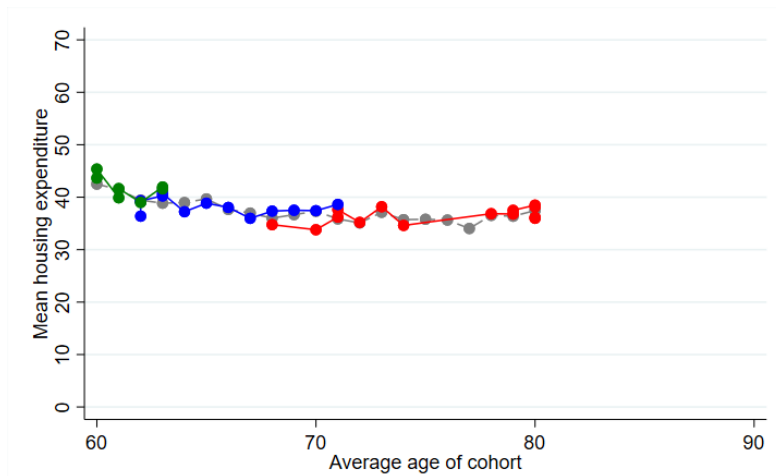
Cohort differences



Notes: LCFS 2003 to 2016

Cohort differences

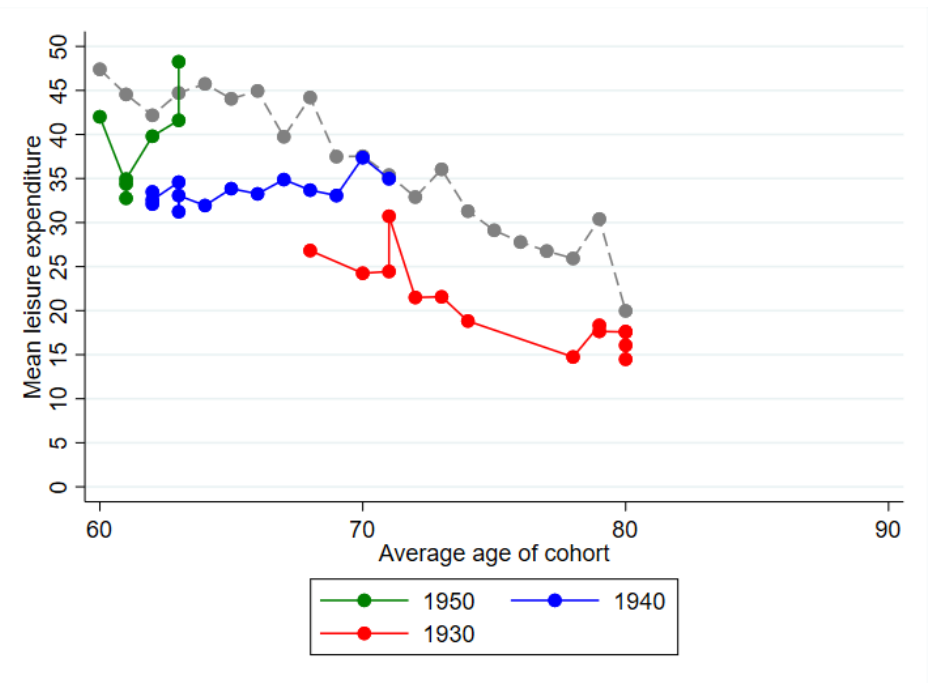
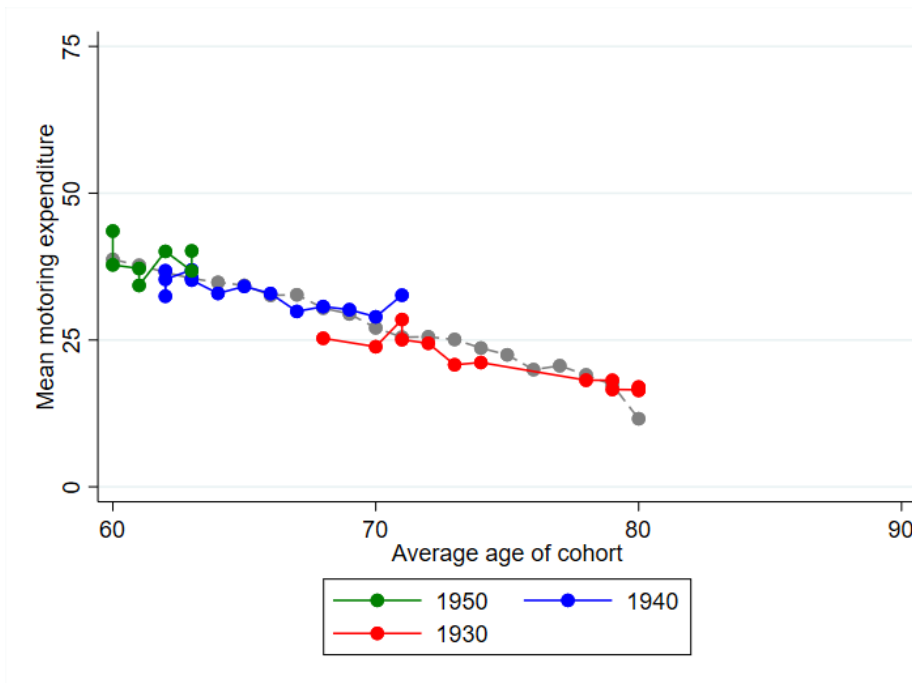
Necessities



Notes: LCFS 2003 to 2016

Cohort differences

Activities outside the home



Notes: LCFS 2003 to 2016

Cohort differences

Summary

- Total expenditure: each consecutive cohort spends more, and age profile of spending among each cohort is relatively flat
- Housing and food inside the house are stable both within and across cohorts
- Leisure services and motoring show both cohort differences and a declining age profile especially within older cohorts

Differential mortality

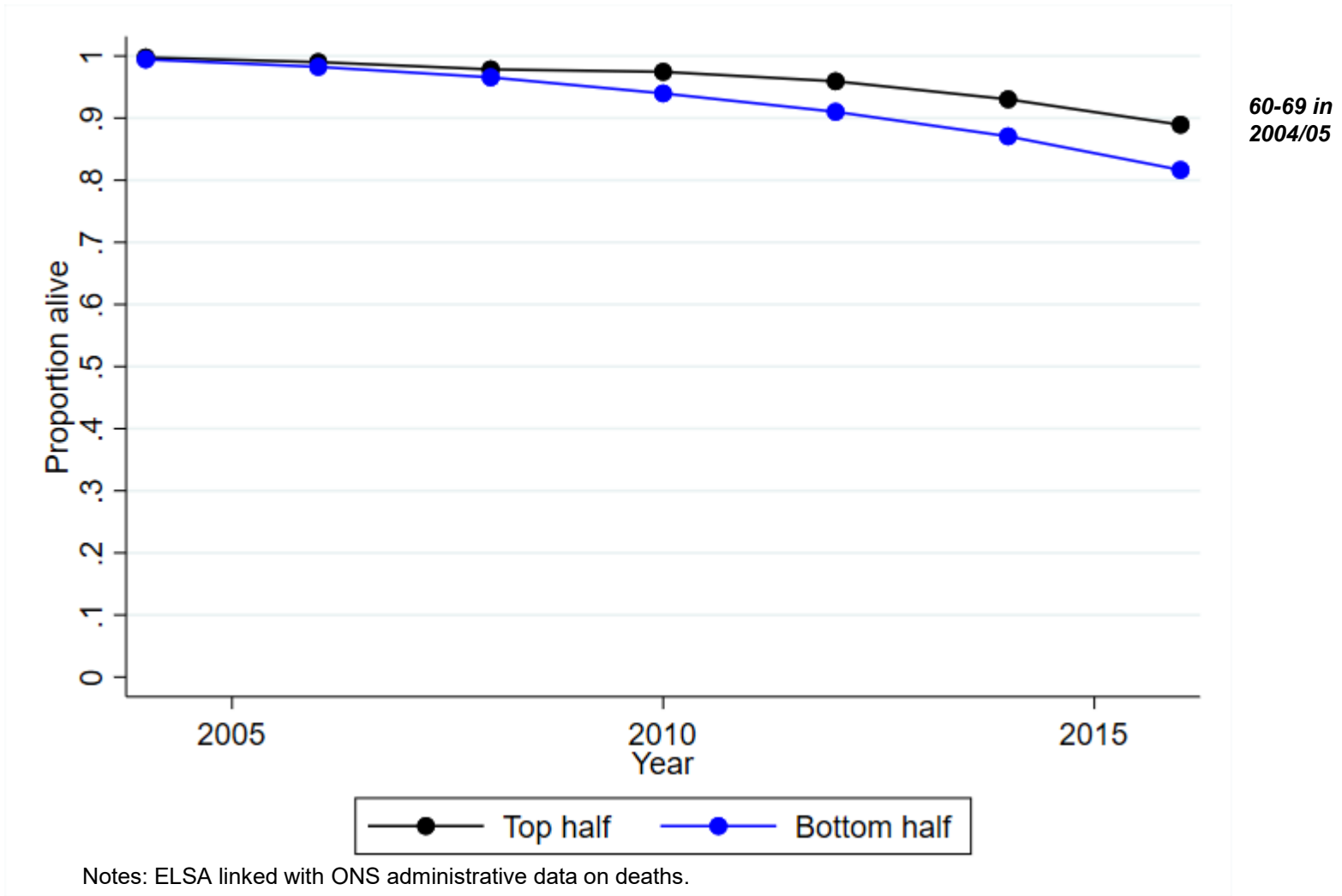
- Cohort profiles of spending may be biased due to differential mortality
- More economically advantaged groups tend to live longer and also spend more
- We can examine this first in ELSA

Dataset: ELSA

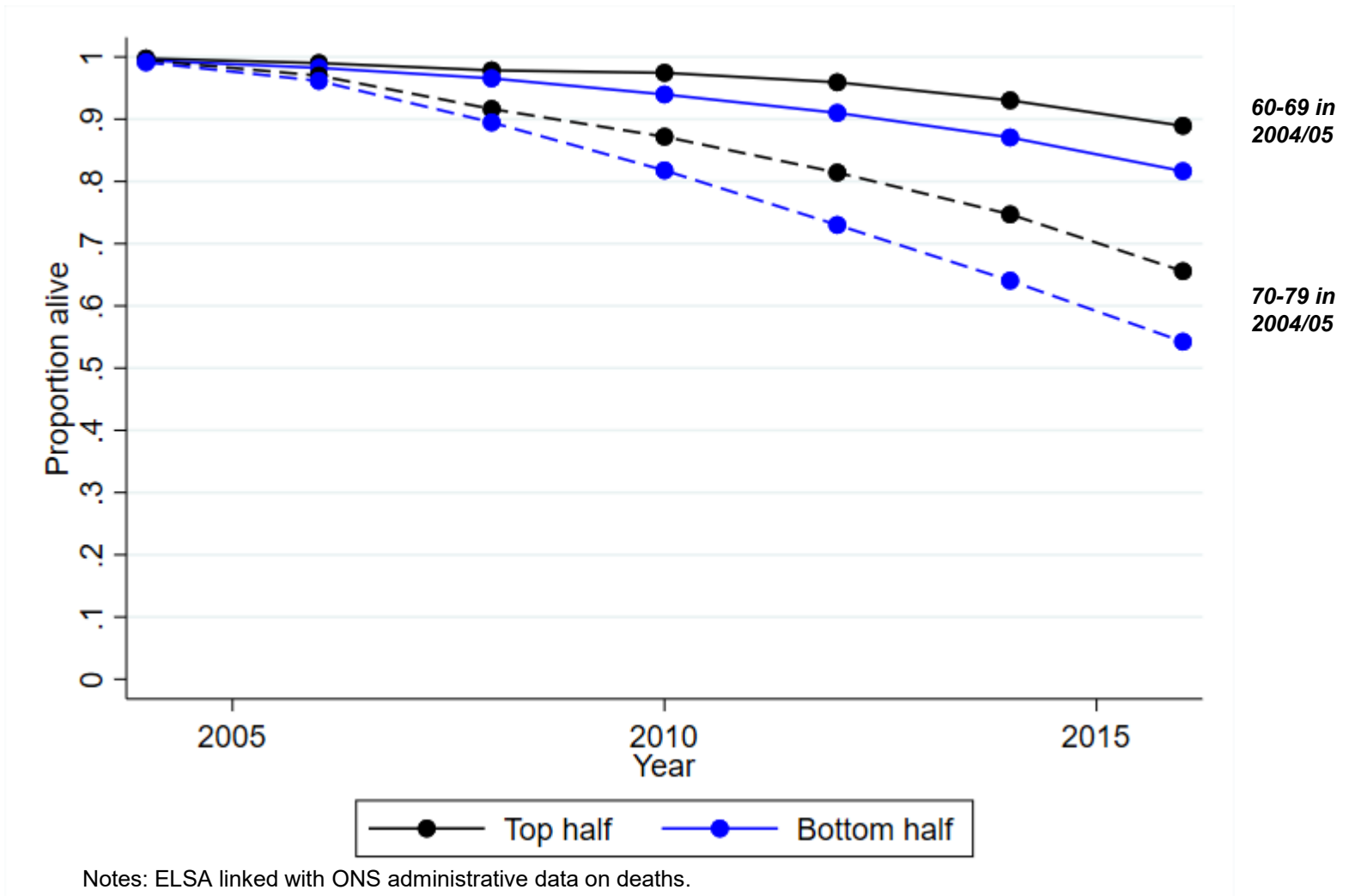


- English Longitudinal Study of Ageing
 - Panel dataset of the 50+ population in England
 - Some recall questions about spending
 - Wide range of household and individual characteristics
- Linked to administrative data on deaths
- We can look at differences in survival probabilities over time based on levels of spending in earlier periods

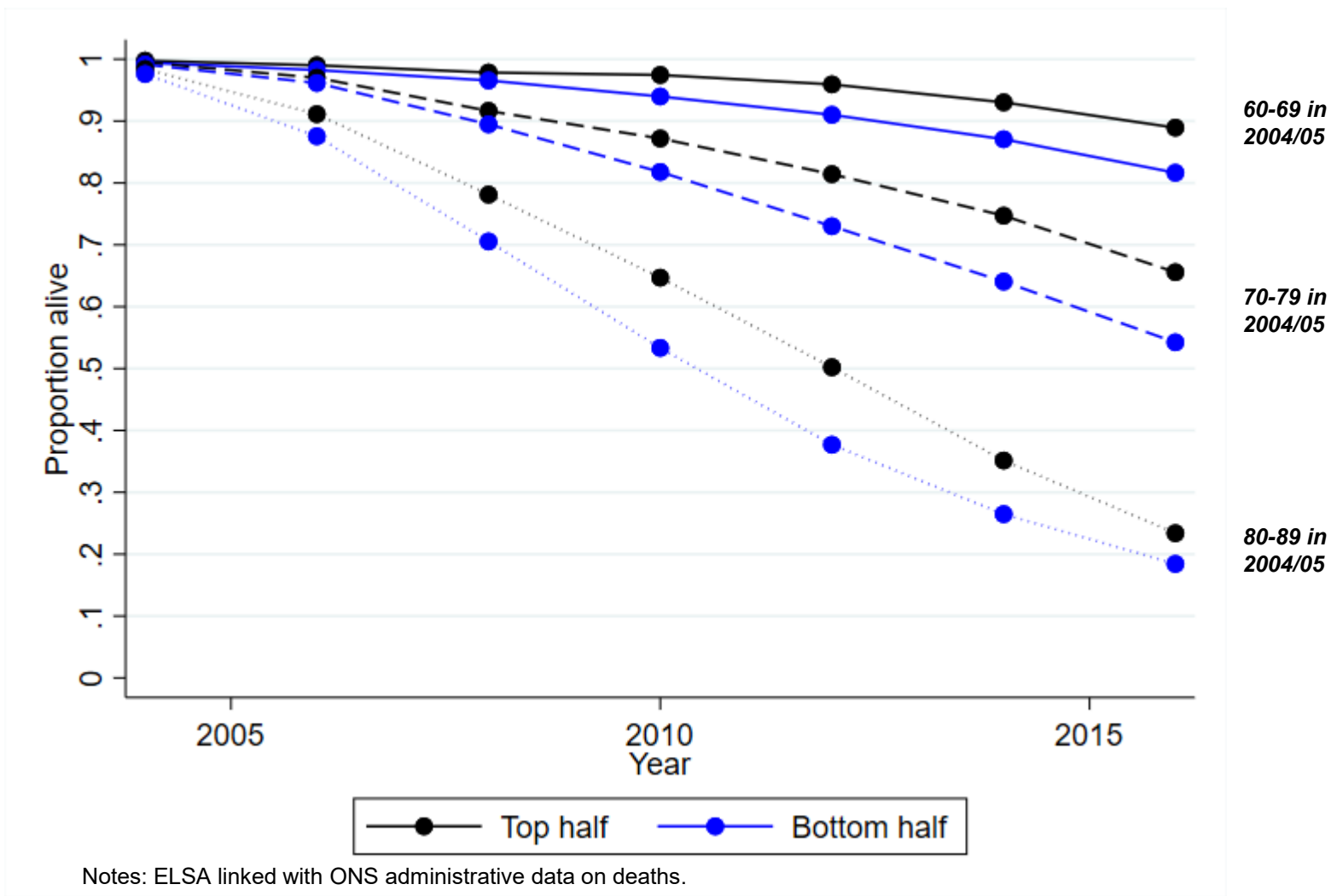
Mortality differs by ELSA leisure expenditure



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Mortality differs by ELSA leisure expenditure

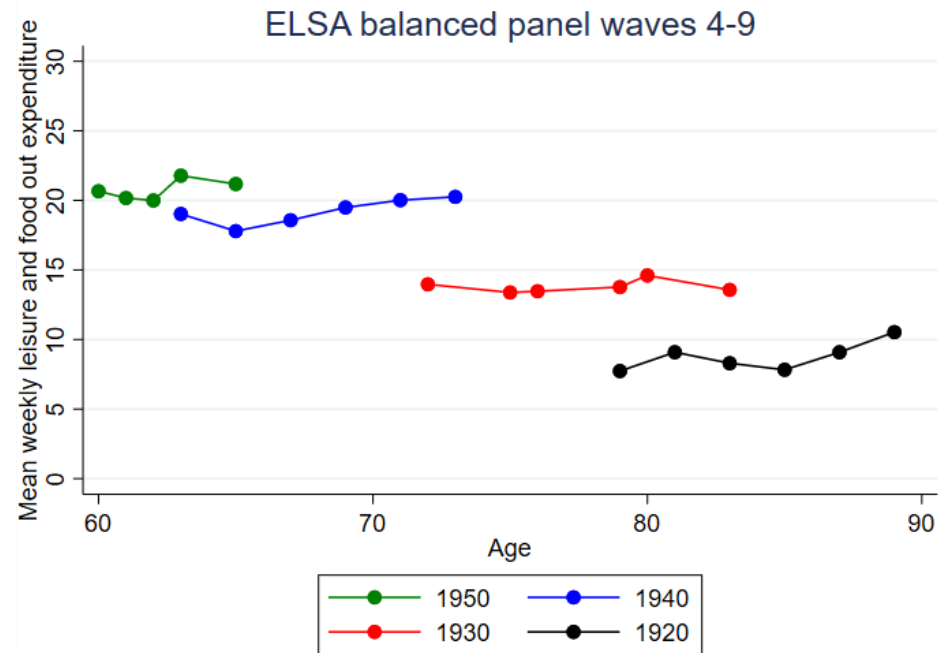
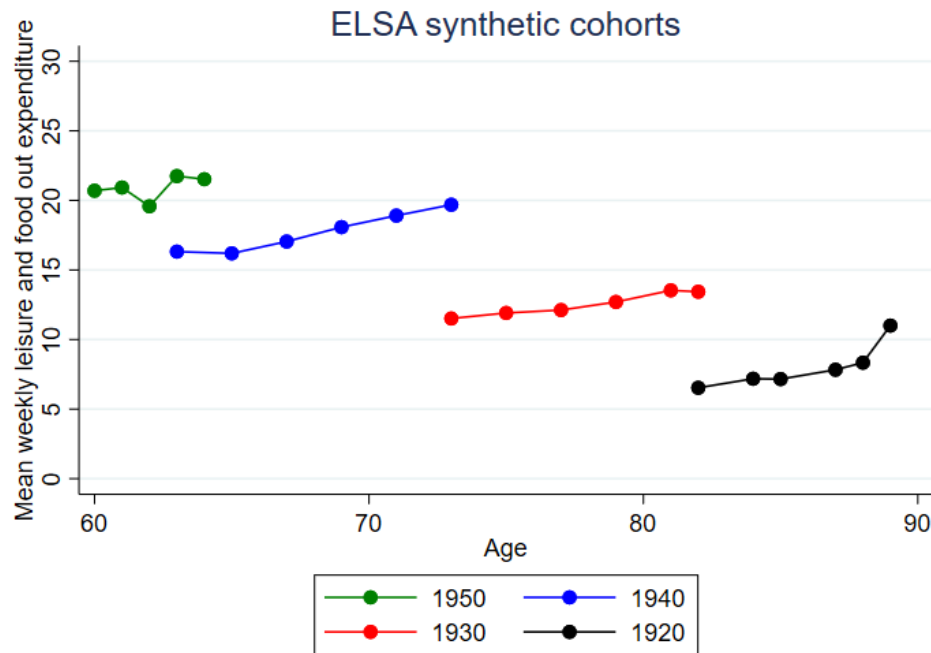


Adjusting for differential mortality

- Balanced panel in ELSA
 - One way to account for differential mortality by using a balanced panel sample
 - Focus on respondents who we observe in all periods

ELSA balanced panel

Leisure and food outside the house



Notes: ELSA wave 4 to 9.

Adjusting for differential mortality

- Balanced panel in ELSA
 - One way to account for differential mortality by using a balanced panel sample
 - Focus on respondents who we observe in all periods
- Re-weighting LCFS profiles
 - We will model mortality based on observable characteristics in ELSA and LCFS, in order to re-weight the LCFS data to account for this

Summary of findings so far

- Cross-sectional average spending seems to fall by age through retirement
- When controlling for cohort differences we find that overall spending does not change as much as the simple age profile suggests
- Differential mortality can also affect the cohort spending profiles, especially among certain categories of spending

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