

UNITED KINGDOM

The UK population has aged considerably over the past 50 years. The figures to the right show the percentage of the UK total population by five-year age groups, separately for males and females. In 1950, the UK population structure formed a classic pyramid, where each successively younger age cohort represents a larger portion of the total population. However, the drop in fertility rates during the Depression and WWII created a slight indentation for several younger cohorts.

By 2000, fertility rates in the UK had decreased from 2.18 in 1950 to 1.61, and life expectancy rose 9 years for both males and females during this period. As a result, the population structure has shifted to a shape that looks more like a pillar, where the population is equally distributed among the age cohorts. The bulge in the middle aged cohorts represents the surge in fertility rates following WWII that produced the baby boom generation.

Looking to the future, the anticipated mix of low fertility rates with rising life expectancy will lead to a fulfillment of a pillar formation. Most noticeable is the spike in the percentage of old age (80+) women in the population. The average age in the UK will be nearly 44 years old by 2030 compared to today's average age of 39.

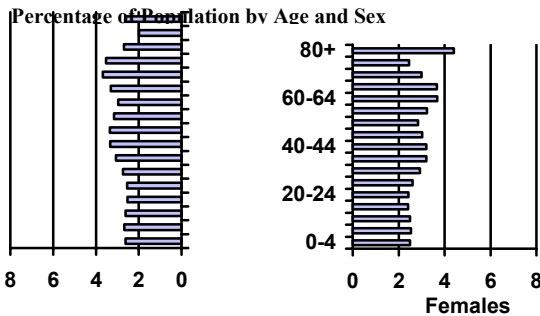
United Kingdom's Population Structure in 1950



United Kingdom's Population Structure in 2000



United Kingdom's Population Structure in 2030



Source: UN Population Division, World Population Prospects (The 2000 Revision).

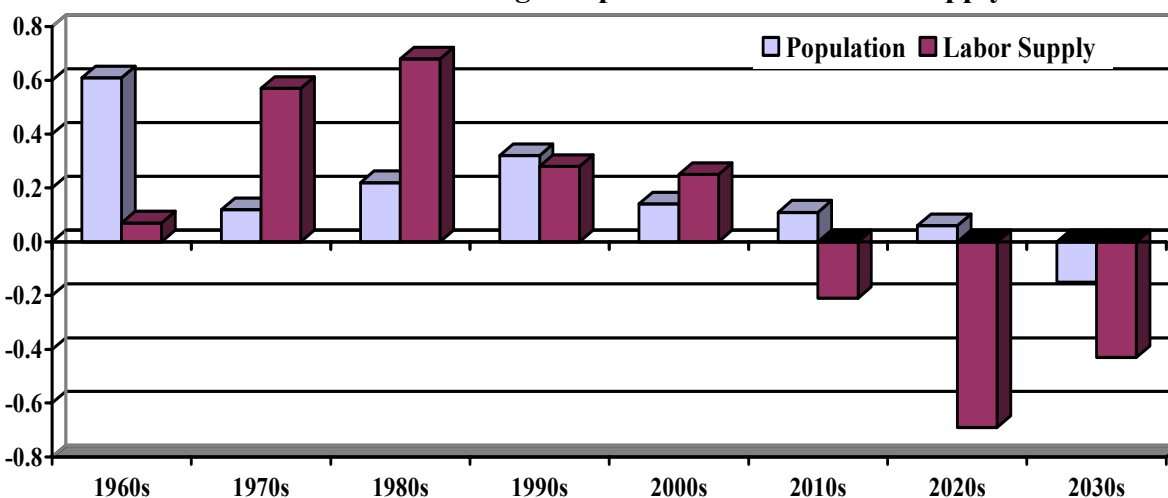
Demographic History

	1950	1960	1970	1980	1990	2000
Life Expectancy at Birth						
Males	66.70	67.90	69.00	71.04	73.65	75.65
Females	71.80	73.80	75.20	77.20	79.04	80.65
Life Expectancy at 65						
Males	-	76.90	77.00	78.06	79.80	80.62
Females	-	80.00	81.00	82.02	83.13	84.17
Fertility Rate	2.18	2.81	2.04	1.80	1.78	1.61
Net Migration Rate	-0.96	0.47	-0.26	-0.01	0.68	0.80

A critical component of a society's ability to expand its production of goods and services is the growth of its labor force. As the UK's population aged over the past half-century, the growth of its labor force has undergone changes as well. Soon after the end of World War II, many industrialized societies, including the UK, experienced a significant spike in birth rates that produced a generation known as the baby boom. While population growth surged in the 1960's, labor force growth remained largely unaffected. However, as the baby boom generation entered the workforce, including an unprecedented number of its female members, labor supply growth expanded rapidly throughout the 1970's and 1980's. Low fertility rates over the last few decades have caused population growth to slow considerably relative to the labor force. This created a temporary boon where a greater percentage of the population was economically active – often referred to as a “demographic dividend”. Between 1970 and 2000, total dependency rates in the UK dropped 13 percent, while youth dependency fell by 29 percent.

As the baby boom generation moves ever-closer towards retirement, labor supply growth in the UK is anticipated to grow more slowly than the population. Prolonged low fertility, increasing life expectancy and a greater proportion of the population falling into age groups that have lower propensity to work, have the combined effect of diminishing labor supply growth. In fact, these factors will actually cause the UK's labor force to shrink, beginning as early as the coming decade. As a result, the UK will face a much greater percentage of its population being inactive, reflected by roughly a 27 percent increase in the total dependency ratio and a 66 percent rise in the old age dependency rate between 2000 and 2030.

Annual Percent Change: Population versus Labor Supply



Source: World Bank, World Development Indicators database

Dependency Ratios

	1970	2000	2030	% change 1970-2000	% change 2000-2030
Youth- (Inactive pop 0-19)/ LF 15+	0.59	0.42	0.38	-28.69	-10.47
Aged- (Inactive pop 55+)/ LF 15+	0.35	0.39	0.65	13.09	66.11
Total- (Inactive pop 0-19 and 55+)/ LF 15+	0.94	0.81	1.03	-13.23	26.47

Source: Sources: International Labor Office, LABORSTA database, current through 2001; UN, Population Division, World Population Prospect (The 2000 Revision); OECD, CDE database on labor statistics, current though 2002

Old Age Pension System

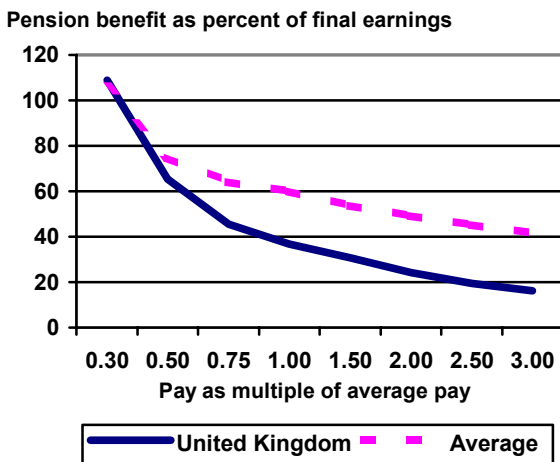
The old age pension system in the UK is two-tiered. The first tier is a flat-rate benefit. To qualify for the full benefit amount, worth £3,510 in 2003, male retirees must have 44 years worth of contributions into the system and be 65 years old, while female retirees need 39 years of contributions and be 60 years old. The qualifications will be equalized gradually between men and women by 2020. A reduced benefit is paid if the criteria are not met, however, credit is given for periods of education, unemployment and disability and caring for children or sick relatives. This basic benefit is indexed to prices and adjusted annually, which will result in a decline in benefits as a share of earnings over time. In addition, there is a means tested supplement, the Minimum Income Guarantee, for retirees with less than £12,000 of savings. This benefit can add up to approximately £400 per month to an individual's basic benefit and £620 per month to married individual's benefit.

The second tier of the UK's old age pension system is an earnings-related benefit known as the Second State Pension (S2P), which replaced SERPS as of April 2002. SERPS benefits were calculated based on lifetime average salary with a targeted replacement rate of 20 percent, paid out after 20 years of contributions. The S2P scheme enhances benefits for low earners by as much as a third or more. The impact of S2P, and SERPS before it, is negligible on the benefits of higher wage earners. For this reason nearly two-thirds of employees in the UK have opted out of this tier and instead participate in an occupational plan, provided by an employer, or a personal pension, purchased from a financial services company. The occupational and private plans are typically defined benefit, but participation in defined contribution schemes has grown rapidly, since the mid-1980s. Both employers and employees pay lower social security contributions when employees opt out of S2P, however, to be eligible to do so, occupational or private defined benefit plans must guarantee a minimum pension benefit and defined contribution plans must impose a minimum contribution. Benefits are required to be indexed to inflation, up to 5 percent per year.

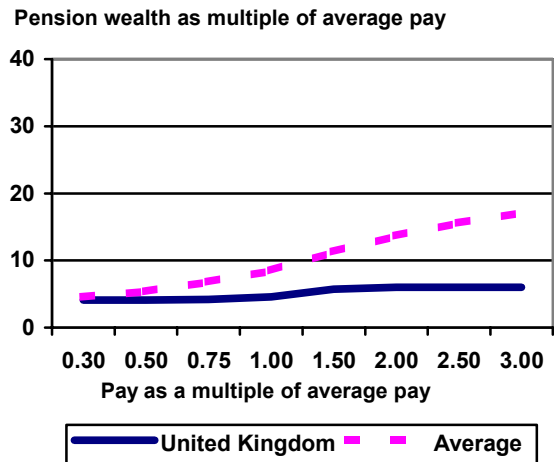
All in all, as indicated by the figures below, the UK's total old age public pension is much smaller in scale compared to other OECD nations. Workers in Britain accumulate much smaller levels of pension wealth under the public pension scheme, especially for employee's making above average earnings.

Source: Whitehouse, Edward (2003), Social Security Administration, Programs throughout the World (2002) and Wyatt Wyatt Data Services (2003) "Benefits Report Western Europe, USA & Canada".

Gross Replacement Rates
United Kingdom v OECD Average



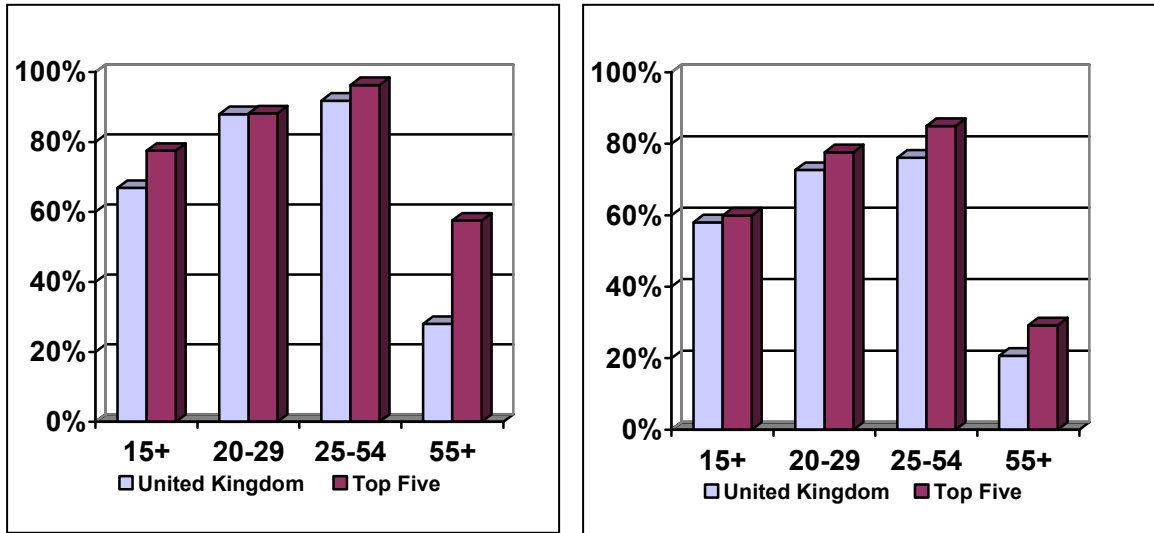
Gross Pension Wealth
United Kingdom v OECD Average



Source: Whitehouse, Edward (2003)

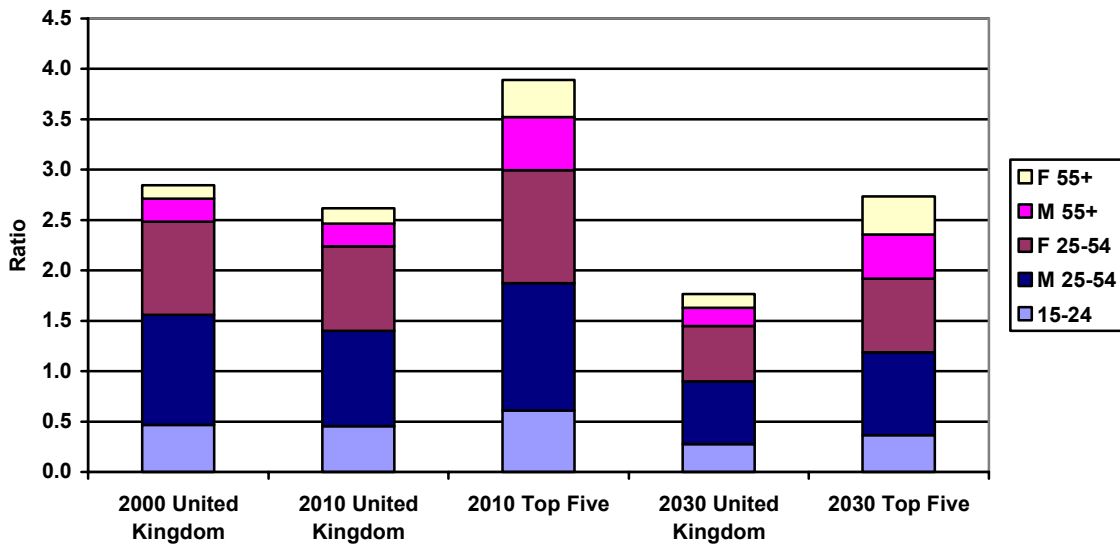
Notes: Pension wealth estimates are a multiple of economy-wide average.

Labor Force Participation Rates: United Kingdom v Top Five OECD Country Composite
 Males Females



Source: OECD, Corporate Data Environment database on labor statistics, current though 2002

Ratio of Workers in the United Kingdom 15+ to Retirees 60+ in 2000, 2010 and 2030 and Under Alternative Assumptions of Old Age Participation Rates for the Top Five OECD Countries



Source: UN Population Division, World Population Prospects (The 2000 Revision); OECD, Corporate Data Environment database current though 2002

Much of the burden caused by demographic aging is due to rising dependency rates. In the coming decades, the UK will need to figure out how to support a growing inactive population with fewer workers. A remedy to this problem is to adopt programs that promote greater workforce participation at all ages. Some countries excel at achieving high workforce participation across various age and gender groups. The figures above show how the UK's labor force participation stacks up next to the average of the Top-five OECD nations. Activity rates in the UK fall short of rates in the Top-five countries for every age and gender group. Most noticeably, older individuals participate in the labor force to a much lesser extent than those in the Top-five countries. If the UK adopts measures to increase labor force participation of older age groups (55+) to rates similar to the Top-five OECD nations, it could significantly reduce its old age dependency rates. As shown in the figure above, if the UK maintains its current activity rates between 2000 and 2030, the ratio of workers to retirees is expected to fall from nearly 2.8 to 1.8. However, by adopting policies to entice workers to defer their retirement at rates similar to those achieved by the Top-five OECD nations, the UK could reduce its dependency burden by raising its activity rate to 2.7 workers per retiree in 2030, nearly matching its current rate.