RETIREMENT INCOME

- A RACE AGAINST INFLATION

The rising cost of living reduces spending power unless your money is growing faster than the rate of inflation.

For those already retired, inflation can affect lifestyle even more than those still working.

While the current rate of inflation is 10.1% the real rate of inflation for retired people can be far higher. That's because while rising petrol prices have been the driver behind the rapid increase in inflation for non-retired households, costs such as energy bills and food make up a greater proportion of inflation for retired households.

Recent figures from the Pensions and Lifetime Savings association (PLSA)[1] have shown that the amount retirees need to achieve a basic standard of living has reached £19,900 a year for a couple - a rise of 19%. The amount for a single person has risen to £12,800, an 18% increase.

The annual increase in what is needed to reach each living standard level over the last year is the largest since the retirement living standards were first established in 2019. Across all the reports, the increase in the price of domestic fuel has been the most significant factor in increasing what is needed overall. Between 2021 and 2022, the weekly cost of domestic fuel rose by around 130%[2].

Whether or not your income in retirement keeps up with inflation depends on the level of inflation at the time, your chosen types of income and how your money is invested.

We explore the different sources of retirement income and ways to combat inflation.

INCOME DRAWDOWN

The flexibility to withdraw as much as you need and leave the rest of your pension savings invested is a helpful way to try and make sure your money keeps growing – and lasts as long as you need it to.

Much of the success of this will depend on how your investments perform. The skill of a professional adviser can prove particularly valuable, as they can work on preserving the value of your retirement pot.

It is particularly important to only take what you need from your pot to ensure your savings will last for the rest of your retirement.

Last year was difficult with global stock markets and the bond market suffering falls. This year could prove challenging again, so it's crucial to have the right investments – and to set the right level of income. It can be adjusted so if you want to review and reduce – or increase – the amount you receive, it can be done.

STATE PENSION

The full amount of the new State Pension is currently set at £203.85 a week. This normally goes up every year. The amount you receive depends on how many years of National Insurance contributions you have made or been credited with.

Anyone who reached state pension age before April 2016 (and receiving the full basic state pension) will get an extra £14 a week[3].

INFLATION-LINKED ANNUITIES

When you buy an annuity, you use a lump sum from your pension pot to buy an income for the rest of your life.

After years of being unpopular because rates were so low, annuities are making a comeback. That won't help anyone who already has an annuity but if you're in the market for one, there's a good opportunity to explore what perhaps some of your money could buy.

Those with an eye on inflation can opt for an index-linked annuity, where the income rises each year in line with inflation which helps with rising costs of living. The downside is that the payouts start at a lower rate. You might prefer to opt for a standard rate and receive more at the outset. It's important to crunch the numbers first and see where the break even point lies.

Once you buy an annuity there's no going back - you cannot get your lump sum back, so it's important to get it right first time. Taking financial advice is crucial. An adviser can also shop around on your behalf to get the best rate available for you.

CASH SAVINGS

Savings held in cash will struggle to keep up with inflation. Even now that interest rates are looking far more attractive, the most generous accounts are still not paying enough to keep up with inflation.

One option might be to reduce income from drawdown and use cash reserves for a time to allow markets to recover.

An adviser will be an invaluable source of advice for how to steer through times of high inflation to ensure your pension lasts as long as you need it to.

[1]https://www.retirementlivingstandards.org.uk/news/rising-prices-add-almost-20

[2]https://www.lboro.ac.uk/news-events/news/2023/january/rising-prices-add-20-percent-cost-retirement/#:~:text=Between%202021%20and%202022%2C%20the,retirement%20between%202021%20and%202022.

[3]https://www.thetimes.co.uk/money-mentor/article/state-pension-increase/