Financial Planning Ltd

The long term costs of pausing pension contributions.

Royal London recently published some startling statistics in relation to how the increasing cost of living and rising mortgage costs are impacting on pension savers: -

· In the past two years, a third (33%) of all workers have investigated reducing or stopping their pension contributions, rising to 49% of workers aged 18-34

· Stopping pension savings may bump up take home pay by £1,404 per annum*, but means losing out on £4,092 pension savings a year for workers earning £35,000

· One in ten (12%) pension savers are reducing the amount they pay into workplace savings

· Cost of living (55%) and, specifically, rising mortgage costs (15%) are two of the main reasons

Decisions taken to boost take home pay in the short term can have **a dramatic impact on people's future wealth**, according to analysis by Royal London.

Reducing or stopping pension contributions may seem an effective solution to current cash flow woes. However, **a short term boost to take home pay impacts the long term pension value**, especially for higher earners, who miss out by almost four times as much.

As you will probably know, pension contributions attract **tax relief** on the money that goes into the pension. If you take the example of a worker earning £35,000 a year and in a workplace pension scheme saving 5% matched by their employer, they could increase their take home pay by £117 per month, or £1,404 a year, if they stopped paying into their pension. However, crucially in doing so they would miss out on £341 per month or £4,092 per year in pension savings, as a result of lost matched contributions and tax relief.

Pension wealth benefits hugely from **compounding**, or to put it another way, the magic of time. The longer money is invested, the more it could grow. In 20 years' time the £4,092 could have boosted the pension pot by £10,575** through investment growth had the contributions not been paused.

For a higher rate taxpayer on a salary of £70,000, the difference is starker. While they could bump up their take home pay by £3,360 a year by stopping 8% matched pension contributions, their pension pot would be worse off by £12,192 in the period. Their pension savings would also be worse off by a projected £31,508** in 20 years' time had they not taken a one-year pause.

The benefits lost by opting out of a workplace pension.

A decision to exit your savings scheme means missing out on the benefits of saving through a workplace pension. To begin with you'll miss out on your employer's contribution. Any breaks in savings could also delay your retirement or mean you'll have less income when you stop working, and catching up on any breaks will mean saving even more when you resume to achieve your desired lifestyle in retirement.

While the number of people opting out of schemes remains relatively low, it's clear that a lot of people have considered the option in a bid to boost their take home pay.

Worker earning £35,000 salary, stopping matched contributions of 5% employee and 5% employer:

Monthly	With contribution	Without contribution
Total monthly contribution	£341	£0
Take home pay	£2,202	£2,319
Difference in take home pay	£117	
Potential missed pension fund growth after 20 yrs**	£10,575	

Worker earning £70,000 salary, stopping matched contributions of 8% employee and 8% employer:

Monthly	With contribution	Without contribution
Total contribution	£1,016	£0
Take home pay	£3,857	£4,137
Difference in take home pay	£280	
Potential missed pension fund growth after 20 yrs**	£31,508	

Assumptions: Employee contribution matched by employer, using salary exchange, all national insurance savings re-directed to member's pension. **20-year projections based on 5% investment growth net of charges.

Justin Corliss, senior pensions development manager at Royal London, commented:

"It will come as a surprise to many just how much you stand to lose by opting out of your workplace pension for one year.

"With the cost of living, driven in particular by mortgage payments and rent, ramping up, workers across the earnings spectrum are having to juggle their finances. However, the decision to pause pension contributions is one that needs to be weighed up carefully, especially for those at the start of their career. Stopping or reducing contributions might be necessary for some, but it's vital that decisions aren't taken on a whim. The figures show that the money gained in the short term doesn't appear great value when compared to what's being given up in the longer term."

If you would like to discuss your retirement plans in more detail and perhaps whether you are saving enough for your retirement, please do get in touch by contacting the office on 0161 839 8229 or rob@mgp-financialplanning.com.