The deficit between retirees' needs and pension provision is growing by $28bn every 24 hours

72.6

GLOBAL AVERAGE LIFE EXPECTANCY AT BIRTH, 2019

As the age of the world's population increases, so does the global pension deficit. Could diverse land and property segments be the long-income assets needed by pension fund investors?

Words: Mat Oakley, Head of Savills UK and European Commercial Research

Every year, the Royal Statistics Society selects a figure that reflects a key issue of the past 12 months. Its international statistic of 2019 was 72.6 years: the estimated global average for life expectancy at birth in 2019. This is the highest ever level, and a dramatic rise from 45.7 years in 1950. Undoubtedly, it's a cause for celebration, but it also raises opportunities for investors in real estate.

While the most obvious opportunity to capitalise on the world's ageing population is through the provision of senior housing and other care facilities, a worrying concern is the global pension deficit and how this will lead to greater demand for long-term secure income streams, such as property.

The challenge is huge. Over-65s account for 19% of the UK population. In Germany, they make up 22%, while in Japan, 28% of the population is aged 65 and over.

Globally, the population of retirees is forecast to grow from 1.5 billion to 2.1 billion between 2017 and 2050. The problem for policy makers is that during the same period the number of workers for each retiree is expected to halve from eight to four, according to the World Economic Forum (WEF).

A combination of factors, such as financial illiteracy, the size of different generations, and declining fertility rates will, the WEF suggests, lead to a global pension time bomb of $400 trillion by 2050 in just eight countries with some of the largest pension markets or biggest populations (Australia, Canada, China, India, Japan, the Netherlands, the UK and the USA). The deficit between retirees' needs and pension provision is growing by $28 billion every 24 hours in those same eight countries, and will be five times the size of the global economy by 2050.

"The anticipated increase in longevity and resulting ageing populations is the financial equivalent of climate change," says Michael Drexler, Head of Financial and Infrastructure Systems, WEF.

However, the potential deficit may not be as large as some suggest. Much of the modelling around 'pension time bombs' is based around measures similar to the old-age dependency ratio. This measures the number of those aged 65+ as a share of those aged 15 to 64. This kind of analysis is worrying for countries such as Germany where the ratio will have tripled by 2060. However, these assume that over-65s are economically inactive. Yet, the statutory and effective retirement ages in many countries have been rising since the late 1990s.

People are working longer for many reasons. There is the pension deficit, where people work because they cannot afford not to. There is also the decline in manual labour and improved mental and physical health in seniors in the developed and developing worlds. For example, philanthropist and investor, Warren Buffett, is 90 this year.

PENSION FUND INVESTMENT INTO LAND AND PROPERTY, BY COUNTRY

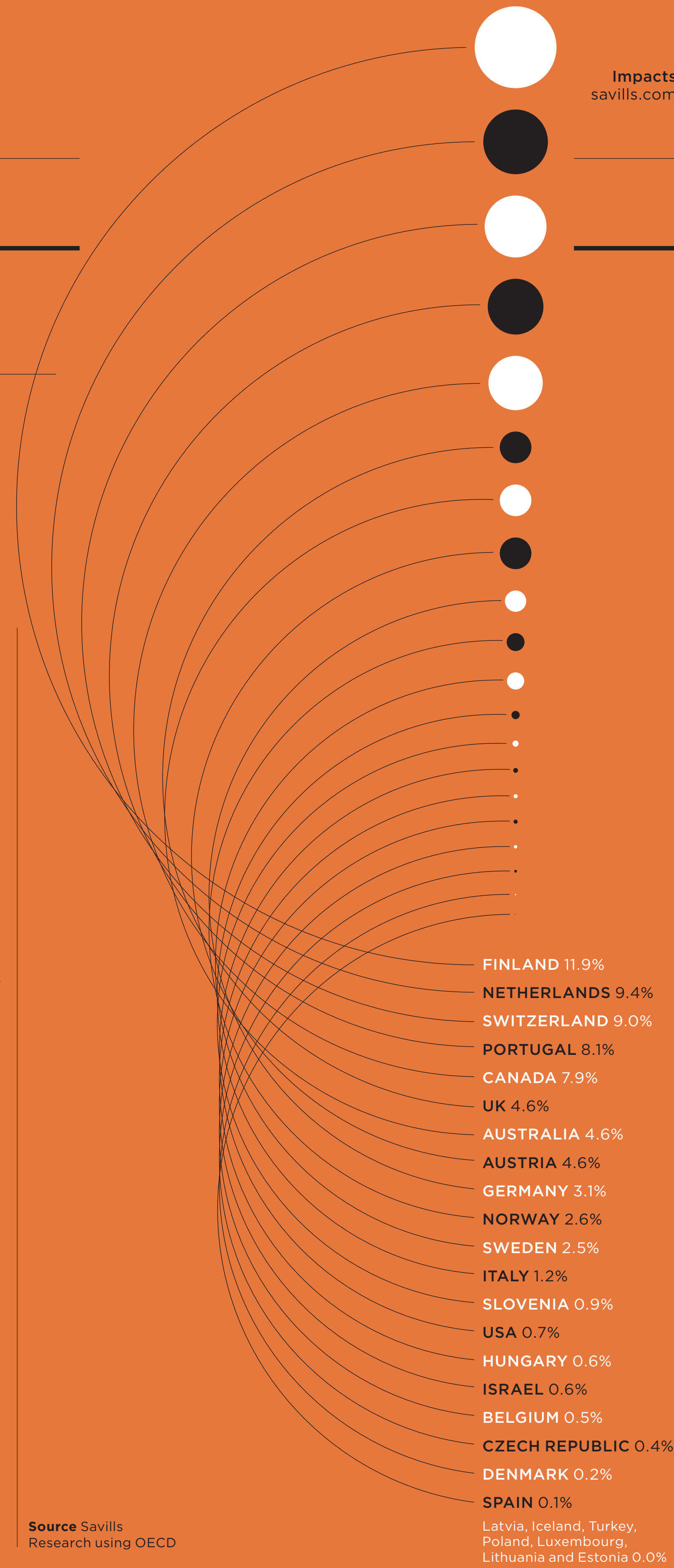
While this is interesting for economists, and challenging for policy makers, why should property investors be thinking about these themes? The main reason is that pension funds have always been significant investors in land and property, and rising needs for more pension provision will mean that more pension and annuity fund money will be targeted at the sector.

According to the OECD, an average of 2.7% of global pension fund assets at the end of 2018 were in land and buildings – a relatively modest allocation, but a significant sum in a total of $44.1 trillion at the end of 2018. This reflects the long-held investor view that land and property are good long-term holds. This leads to why I think an ageing population will be good for property investors.

The challenge for the world's pension fund investors over the next decade is going to be a scarcity of long-income opportunities. The disruption of traditional retail and office models by companies such as Amazon and WeWork has driven a steady decline in the average lease length attached to a typical property investment. I expect that this will continue to shorten, which will mean that the largest and most liquid parts of the market will no longer offer the level of annuity-matching that they used to.

As interest in the old core sectors has declined, so it has risen in new alternatives. According to Real Capital Analytics, total global investment into offices increased by 10% during the past three years, while investment into residential grew by 17%, and senior housing and care by 22% during the same period. The challenge for investors is that many of these sectors are small, specialist or illiquid. While there might be a desire to buy these segments, the reality of getting invested is challenging.

Rising demand for longer-income assets will, I believe, meet a falling supply and a rise in prices. This means it will not only be senior housing that benefits from an ageing population, but segments as diverse as pubs, logistics, data centres and offices. ■



Source Savills Research using OECD