



Retirement Incomes: Thoughts on Future Public Policies

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Agenda



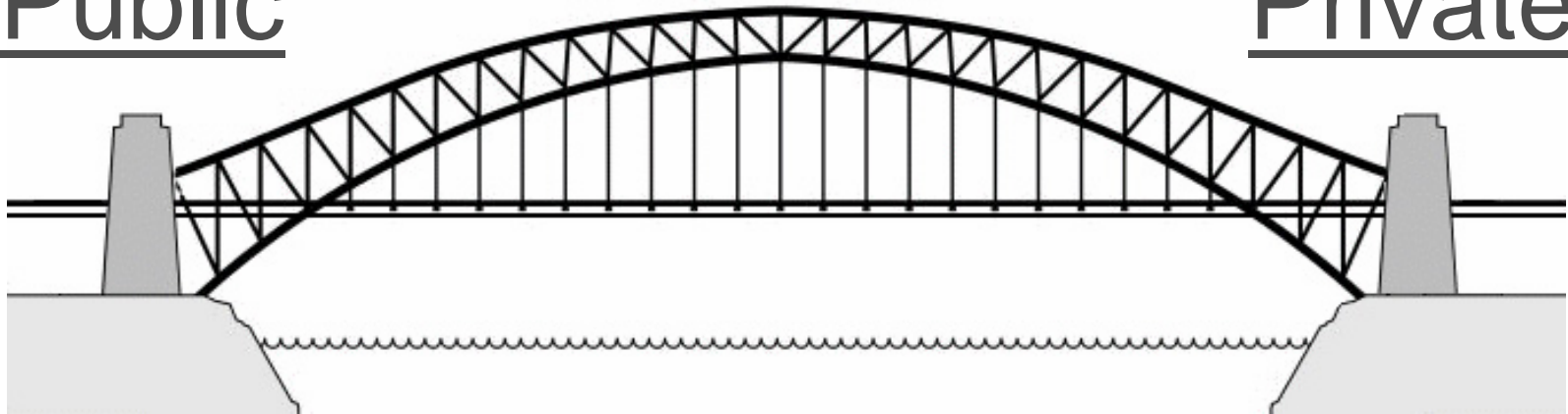
- **Retirement income solutions – a joint product of government policy and the industry**
- **Demographic changes – growing urgency**
- **Taking a system wide perspective**
- **Understanding net worth**
- **Some potential policy considerations:**
 - Taxation
 - Private annuities
 - Home ownership

Public / private Integration



Public

Private



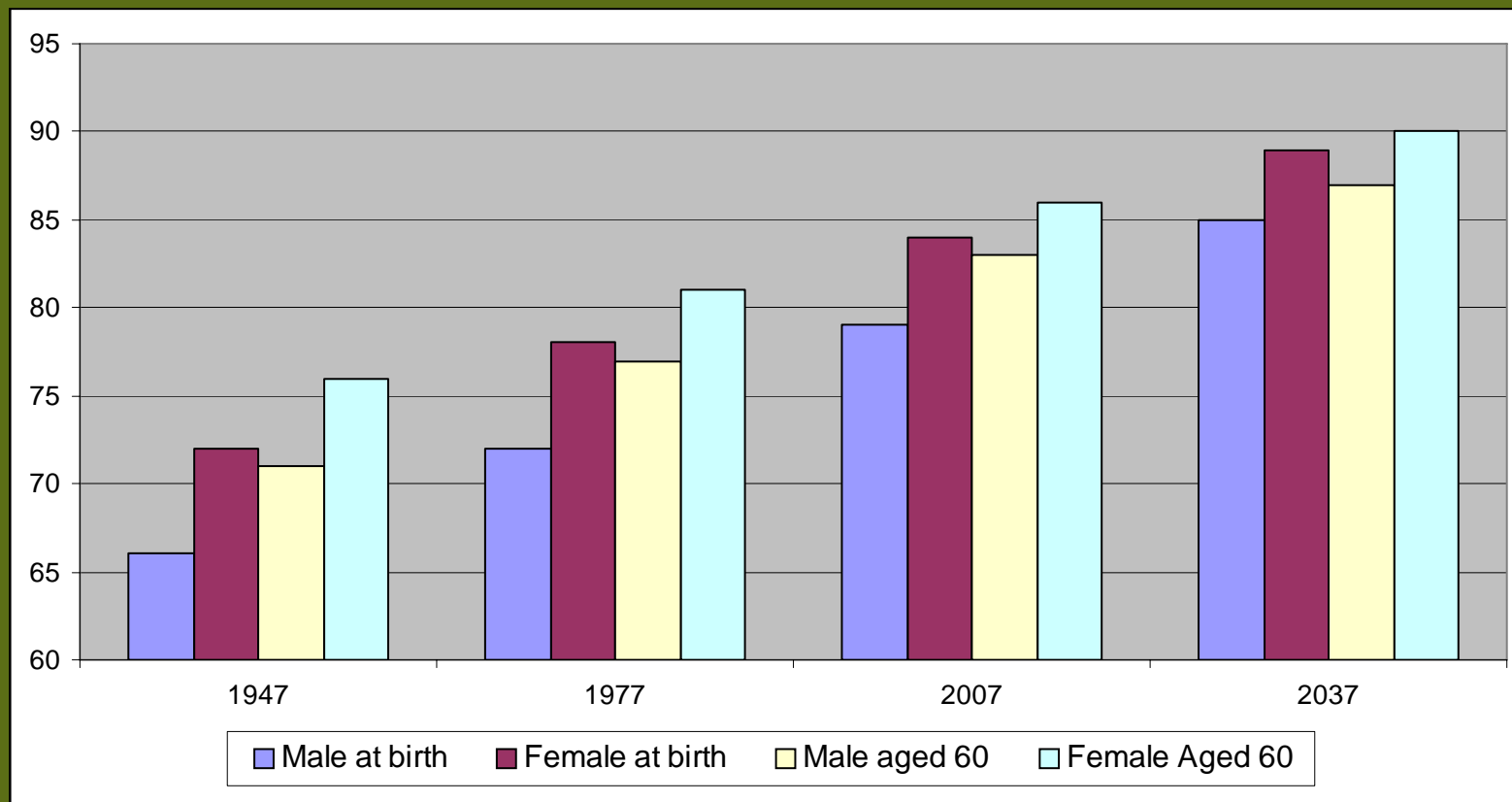
- Market failure
- Incomplete markets
- Redistribution

- Innovation
- Efficient resource allocation

Australia's demographic position



Longevity risk - life expectancy is increasing

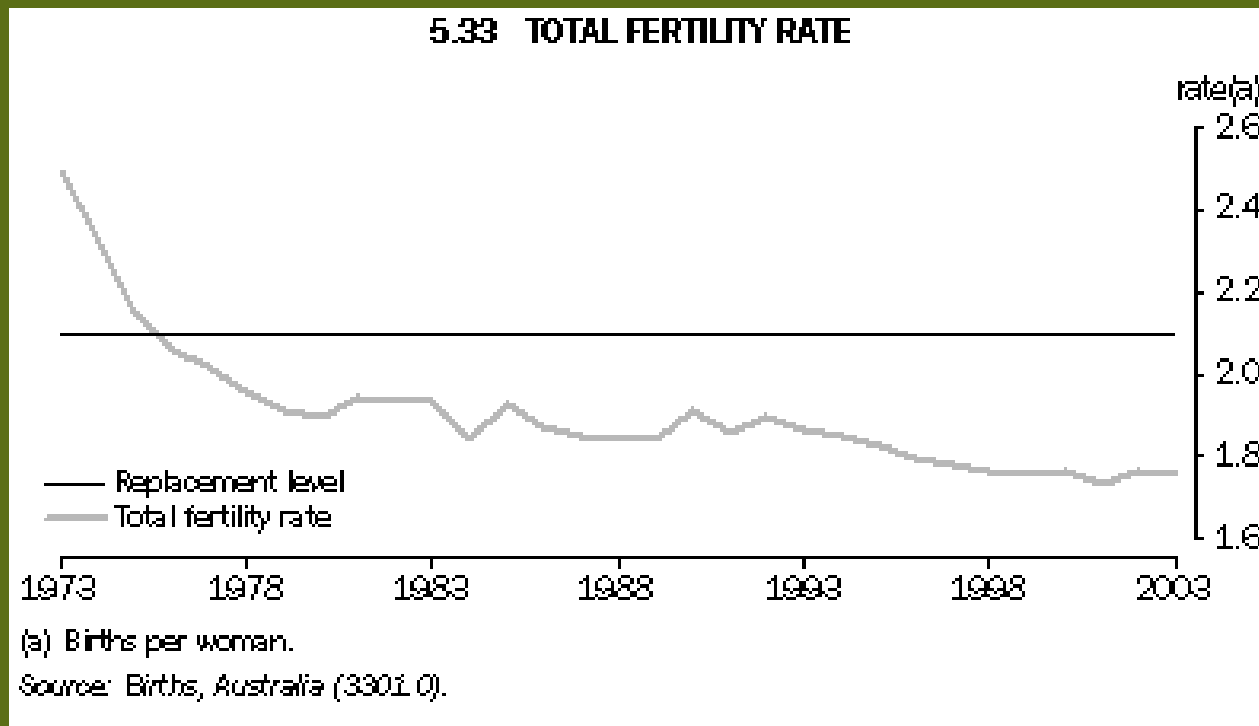


Sources: Australian Bureau of Statistics & 2007 Intergenerational Report

Australia's demographic position



Longevity risk – fertility is decreasing

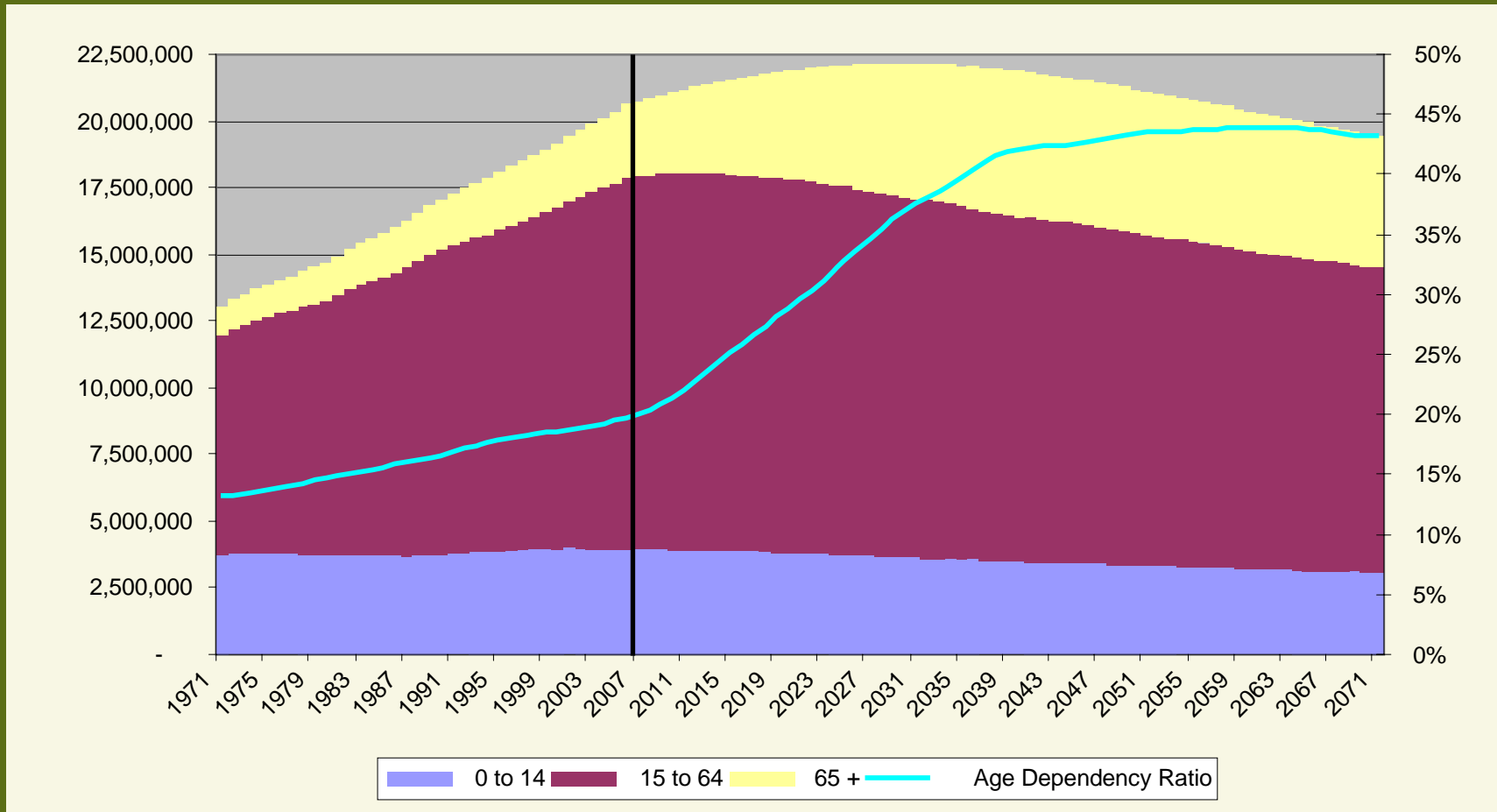


Source: Australian Bureau of Statistics

Australia's demographic position



Age dependency ratio will soon increase rapidly



Sources: Australian Bureau of Statistics (1971 to 2007) & BGI forecast (post 2007)

Australia's three pillar super system



Pillar 1

Publicly managed tax-financed pillar providing a social safety net and redistribution



Pillar 2

Mandated, fully funded and privately managed DC pillar that links benefits to contributions

Pillar 3

Voluntary, fully funded and privately managed pillar for people who want more protection in old age

Retirement solutions affect all age cohorts



- **Public PAYG defined benefit systems can have the following problems:**
 - High and rising payroll taxes that may increase unemployment
 - Evasion to the informal sector
 - Early retirement
 - Unintended inter-generational transfers (often to high income groups)
 - May not be sustainable

The importance of the “All Assets Plus Liabilities” perspective



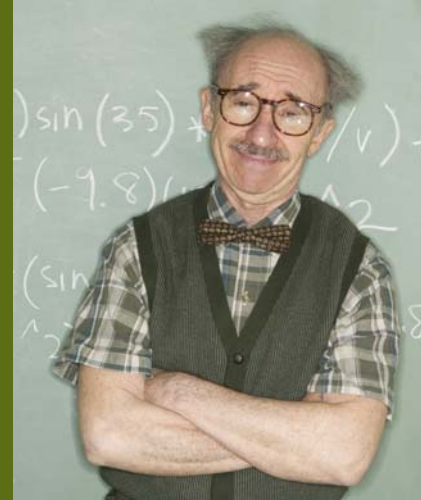
Accumulation

- Human capital
- Home ownership
- Superannuation
- Other assets



Retirement

- Home ownership
- Superannuation
- Age pension
- Other assets



- Govt policy
- Tax system

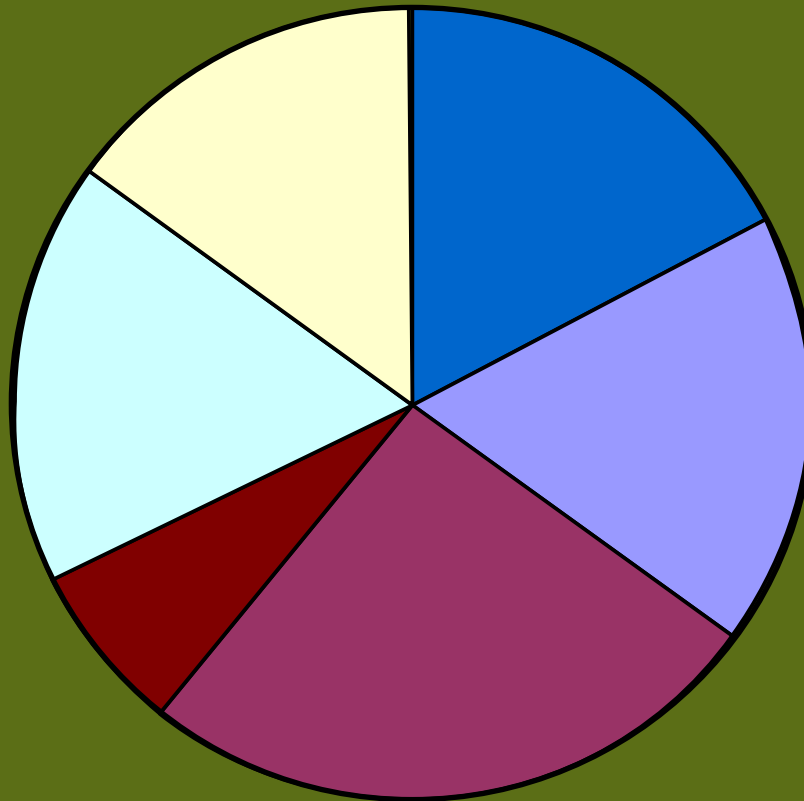
Government

- Govt support / Age Pension
- Govt policy

Net worth of the “typical” Australian approaching retirement



~\$650k

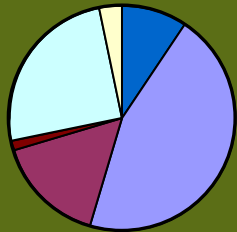


- Super
- Age Pension
- Own home
- Investment property
- Human capital
- Non-super financial assets

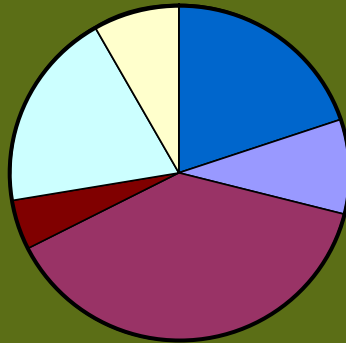
Net worth of the “typical” Australian approaching retirement



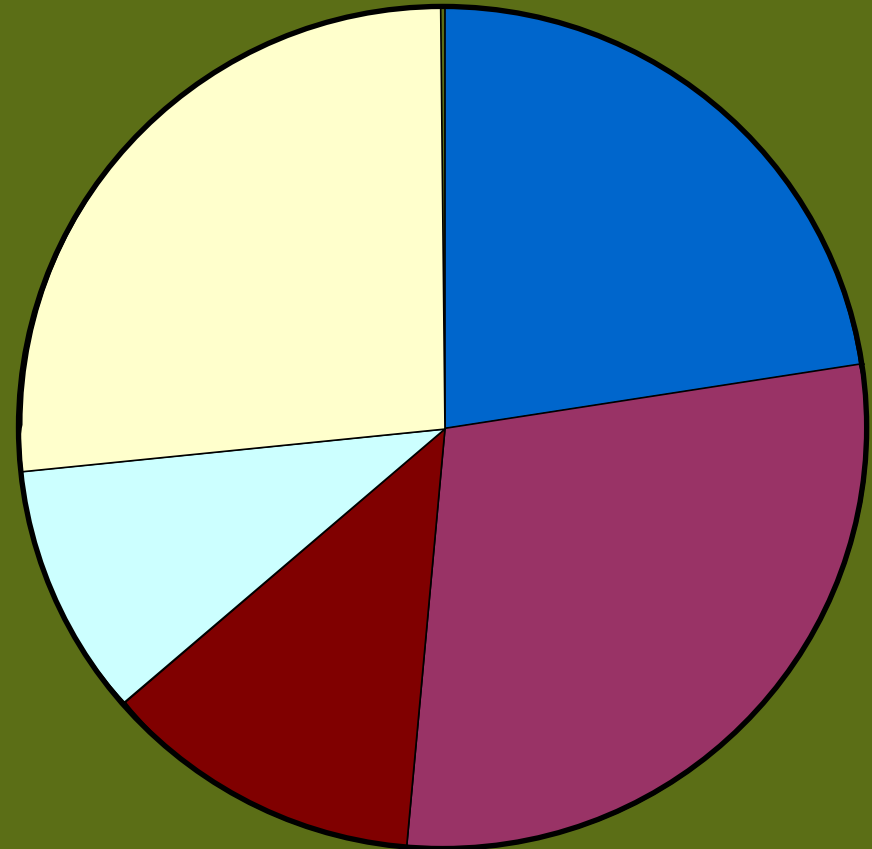
Q1–Q3
~\$400k



Q4
~\$600k



Q5
~\$1.5m



- Super
- Age Pension
- Own home
- Investment property
- Human capital
- Non-super financial assets

Some potential policy considerations



- **Taxation**
- **Private annuities**
- **Home ownership**

Taxation of Super



Taxation of gains in managed funds and superannuation creates complexity, fragmentation and perverse incentives

- unit holder tax affected by other unit holders, change in managers and product innovation
- uncertain revenue vs capital distinction
- time varying penalties from active management
- incentive to defer realisation nearing retirement

Taxation of Super

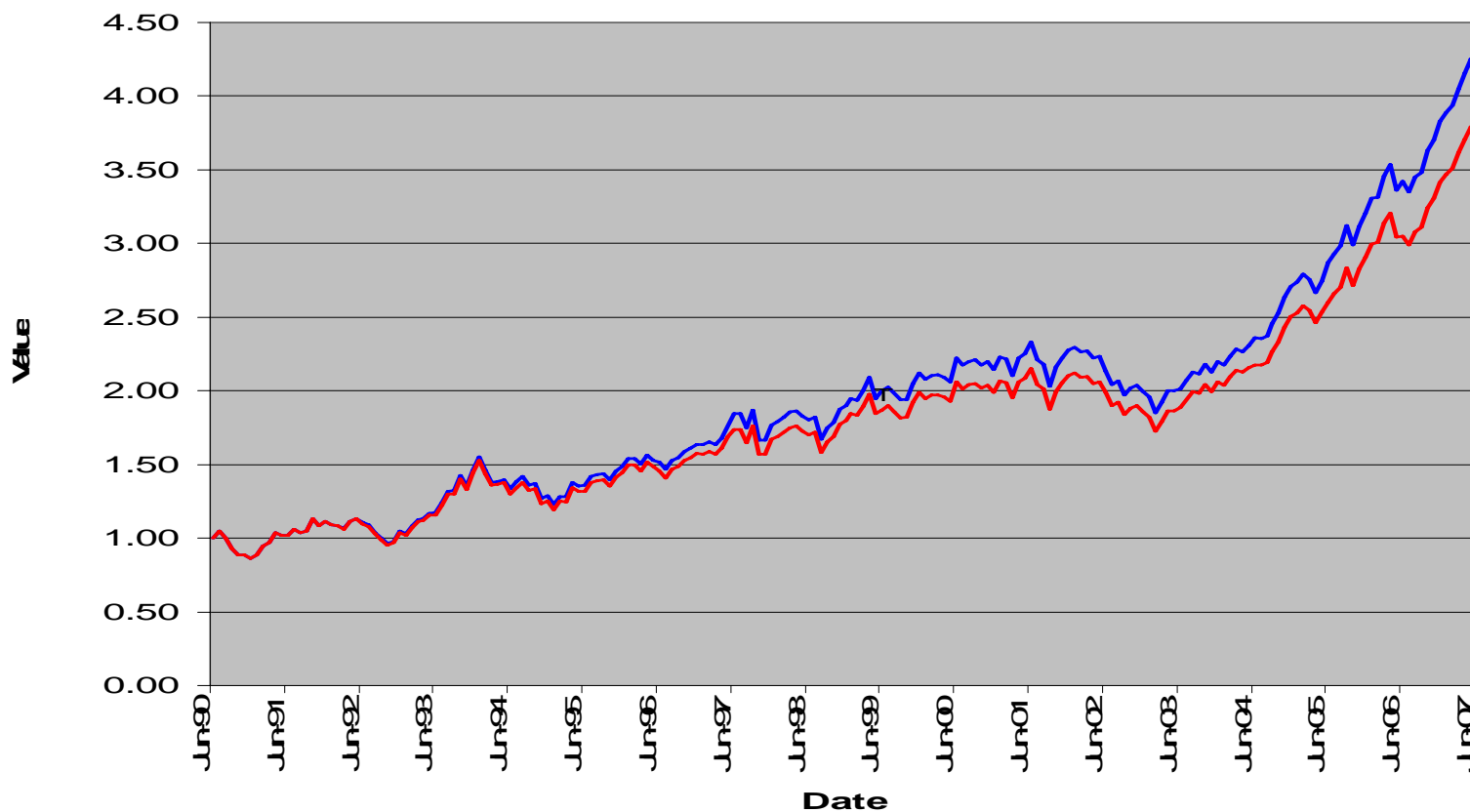


- **Put all managed investment funds on capital account**
- **Tax unit holders on gains only on sale of units, eliminate fund distributions of gains**
- **Defer capital gains tax in super funds until assets are transferred to the pension account**

Taxation of Super



Australian Equity Performance 1990-2007



Private annuities



- **Market failure: mandate life annuities as a component of pension account?**
- **Incomplete markets:**
 - Government to issue inflation-linked bonds
 - Government to provide mortality statistics and risk insurance
- **Investor protection:**
 - Clearing market for annuities
 - Regulatory capital model – provide affordable bankruptcy protection

Home ownership



Home ownership encourages saving, provides a life annuity indexed to the cost of housing services and has a residual value expected to grow

- Access Super to increase home ownership
- Facilitate the market for reverse mortgages
- Review Age Pension and rent assistance mix

Conclusions



- **The baby-boomer retirement wave is imminent**
- **Segments (wealth and home ownership) will require different products and support**
- **A successful retirement system is a joint product between government and the industry**
- **Opportunities for policy development lie with taxation of managed funds and superannuation, the market for life annuities and retirement strategies linked to home ownership**