The Australian retirement industry

Catherine Nance
PricewaterhouseCoopers
July 2008
Australia in 2050
Australian population in 2050

Population of 28 million:
- Median age is 45
  - 50% over age 45
  - 26% over age 65
  - 6% over age 85

In 1920s-1930s
- The median age was 25
  - age 25
  - age 45
  - age 65
Companies in 2050

Post war ageism has vanished
For past 50 years
• 70% of workforce growth has come from over 45s
• 10% from 15-24

Company focus
• Attracting and retaining over 45s and females
Individual attitudes 2050

At 65, expect to live another 25-30 years
- Plan to keep working at least another 10 years
- Move onto Age Pension from around 75-80
- Savings plus AP will provide “adequate” retirement income
- House will fund Aged Care entry when required
Australia’s finances in 2050

Workforce participation rates
• 90% for 25-64 year olds
• 66% for 65-74 year olds

2007 participation rates (males)
• 90% for 25-54 year olds
• 66% for 55-64 year olds

Manageable health costs
Manageable age pension costs
Where are we now?

Population of 21 million with median age of 37

Companies

- Ageism exists
- Focus on youth, Gen X and Gen Y
- ABS stats on turnover
  - 25% pa for 20-25s
  - 6% pa for over 45s
- Early stage awareness of demographic changes
Individual attitudes 2008

At 65, we live another 20-25 years
Aim to retire around 55+
  - Actual retirement is 61 males and 58 females
Expectations are big!
• No concept of our longevity
Dreams

What do we want?
Individual attitudes 2008

Recent international survey of 12 nations* showed that Australians ....

• Were looking forward to their retirement ✓
• 50% expected to live comfortably in retirement ✓

Survey also showed that Australians ....

• Had no idea what savings are needed to live comfortably in retirement
• Had no idea of what savings they will even have at retirement

*AXA retirement survey 2006
What does it take to live post 60?

Modestly
$26,000 p.a. couple
$18,000 p.a. single

Comfortably
$48,000 p.a. couple
$36,000 p.a. single

*Westpac ASFA Retirement Standard research report 2007
The reality

Super savings for recent retirees
• $136,000 males
• $63,000 females

Percentage of people with super > $100,000
• 8% of males
• 4% of females

80% of Australians over 65 rely on the Age Pension
• 55% rely on full Age Pension
The reality of living post 60?

Modestly

$26,000 p.a. couple
$18,000 p.a. single

Comfortably

$48,000 p.a. couple
$36,000 p.a. single

AND THAT’S WHILE WE ARE FIT AND HEALTHY…..

Age pension

$24,000 p.a. couple
$14,000 p.a. single

*Westpac ASFA Retirement Standard research report 2007
2004-05 health snapshot for >= 65s (ABS)

- 100% had at least one health condition
- 68% self assessed as in good health
- 13% of those over 65 have diabetes
- Around half suffer arthritic conditions
- 48% overweight or obese
- 11% living with psychological distress
- 8% still smoking
- 4% of over 75 had an injury due to falling over in past four weeks
- Around a quarter over 65 had been in hospital in previous 12 months!
- 82% of those over 85 had a reported disability
The reality

Home ownership for over 65s

• 85% couples own a home
• 74% of singles own a home
Seniors typically have low incomes – but lots of assets

Mean gross household income by age group*, 2003-04

Mean household net worth by age group*, 2003-04

* Age of ‘reference person’ (household head).
The Reality

What will we get?
Australia’s finances 2008

Workforce participation rates
- 90% for 25-54 year olds
- 66% for 55-64 year olds

Very limited work beyond age 65
- Age Pension is not integrated with work
Marginal tax rates with Age Pension Income Test

Income test reduction 40% (less tax)

Marginal Tax Rates

Income ($'000)

Age Pension

MTR less LITO and SATO

MTR less LITO, SATO and AP reduction

MTR less LITO
Intergenerational Reports 2002 & 2007

Warning!!

Source: Intergenerational Reports 2002 and 2007, ANZ Economics
Financial products in 2008

No market in lifetime annuities since Sept 2007
• Up front capital pmt, “expensive” and loss of capital on death

Fixed term annuities - Leaves longevity risk with retiree
Reverse mortgages small but growing, concerns with
• Regulation, disclosure and complexity
• Not integrated with Age Pension

Account based pensions**
• Longevity, inflation and investment risks with retiree
• Outcome being over or under spending in retirement
## Account based pension longevity risk
Rawlinson and Cater 2008

<table>
<thead>
<tr>
<th>Male Currently Aged 60</th>
<th>Likelihood that Allocated Pension will be depleted</th>
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<tbody>
<tr>
<td></td>
<td><strong>50% Growth Assets</strong></td>
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<tr>
<td></td>
<td>0% chance of fund being depleted before this age</td>
</tr>
<tr>
<td>1 in 20 chance of dying before age</td>
<td>66</td>
</tr>
<tr>
<td>1 in 4 chance of dying before age</td>
<td>78</td>
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<tr>
<td>1 in 2 chance of dying before age</td>
<td>86</td>
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<tr>
<td>3 in 4 chance of dying before age</td>
<td>92</td>
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<tr>
<td>19 in 20 chance of dying before age</td>
<td>100</td>
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</tbody>
</table>

ALT00-02 with mortality improvements
How do we move from 2008 to 2020+

What is the potential market for financial products in Australia?

• Numbers of retirees

What might be the demand?

• Financial wealth of retirees
Number of over 65s

NOW popn 21m

2.7
13%

2051 popn 28m

7.3
26%

ABS 3222.0 Population Projections, Australia, 2004–2101
Future wealth in retirement

- Age Pension
- Mandatory Super 9%
- Voluntary Savings
Future wealth in retirement

Age pension will remain a primary pillar for over 65s
• 75%* will rely on all or part Age Pension in 2050*
• Those on full Age Pension reduce from 55% to 35%

Market potential
• 25% self funded retirees
• Median to Average income groups
  - SG account balance $200,000 - $300,000
  - Many will end up on 100% Age Pension

Example:
Median income (75% AWOTE), 9% SG 40 years

- Annual income $26,000 in retirement (65% pre ret income)
- Plus $50,000 lump sum

ASIC retirement calculator
Example:
Average income (100% AWOTE), 9% SG 40 years

- Annual income $38,000 in retirement (comfortable, 62% pre ret income)
- Plus $50,000 lump sum
Issues impacting demand

“The last cheque you write should be to your undertaker… and it should bounce.”
Stephen M. Pollan

Retirees face significant risks managing their assets

- Longevity, early death, investment and inflation
- Lumpy cash flow needs eg aged care
- Credit/provider risks on long term products
- Home equity release risks

Retirement super savings are growing but not large
Many will be on an Age pension annuity
Current product development

Capital market options

• Lifetime pensions
  - Difficult unless transfer/ hedge longevity and inflation risks given capital requirements
  - Size of market??
• Investment guaranteed products
  - Cost of guarantee??
• Pooled lifetime annuity products
  - Size of market, marketability and credit risks???

Account based pensions with default options

• Most likely shorter term development
Current policy ideas

Government options
- Deferred Age Pension
- Remove income testing from means testing
- Increase Age Pension age
- Increase single Age Pension
- Can government take on any more longevity risk??
  - Already longevity insurer for most Australians
  - Issue longevity bonds
  - Allow purchase of Age Pension
How do we move from 2008 to 2020+
How do we move from 2008 to 2020+
How do we move from 2008 to 2020+

Savings need to increase - current focus is on adequacy
Work needs to continue beyond age 61
  • Employer attitudes to change
  • Individual attitudes to change
Age pension needs to drive positive not negative behaviours
  • Integrated with work and savings
Financial products are needed
  • Enable people to manage their post age 65 risks
  • Integrated with phasing up and down of work
  • Lump sum needs inconsistent with over-annuitising wealth
  • Integrated with Age Pension
  • Simple to understand and secure long term products