

# The Australian Superannuation Industry

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**Development of the Australian Financial Market and Its Implications for Korea  
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# Outline

- Motivation
- Structural overview
  - Four pillars
  - Size
  - Contributions
  - Funds
- Investment
  - Large funds
  - Self-managed funds
  - Net returns and fees
- Benefits and Adequacy
- Current changes and concerns

# Populations are aging in Australia and Korea.

## *Australia*

- Current population: 23m
  - 2056 projected: 35.5m
- Current >65 years: 3m
  - 2056 projected: 8m
- Current dependency: 20%
  - 2056 projected: 40%
- Fertility
  - 1.8 births per woman
- Net migration
  - Around 180K p.a.

## *Korea*

- Current population: 50m
  - 2050 projected: 50m
- Current >65 years: 5.5m
  - 2050 projected: 15m
- Current dependency: 17%
  - 2050 projected: 66%
- Fertility
  - 1.3 births per woman
- Net migration
  - < 100K p.a.

# Melbourne Mercer Global Pensions Index rankings of country systems 2012.

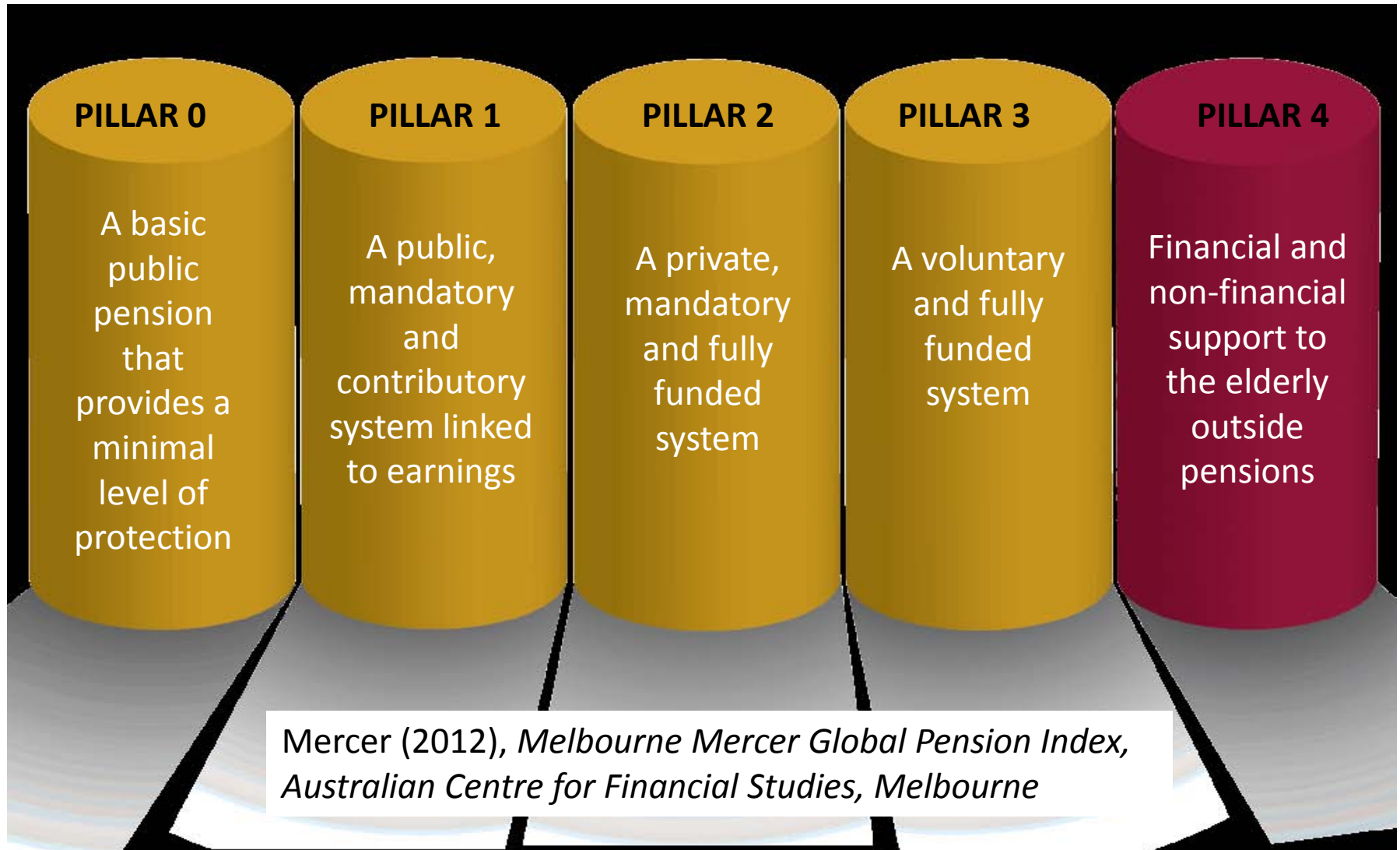
Country	Overall Index Value	Sub-Index Values		
		Adequacy 40%	Sustainability 35%	Integrity 25%
Australia	75.7	73.5	73.0	83.2
Brazil	56.7	71.5	26.9	74.8
Canada	69.2	74.2	56.3	79.3
Chile	63.3	50.1	67.7	78.4
China	45.4	55.7	30.5	49.7
Denmark	82.9	78.1	86.0	86.4
France	54.7	74.3	32.0	55.2
Germany	55.3	65.2	35.9	66.7
India	42.4	37.4	40.7	52.8
Japan	44.4	46.1	28.9	63.3
Korea (South)	44.7	45.1	42.3	47.5
Netherlands	78.9	77.0	73.0	90.3
Poland	58.2	63.6	43.4	70.1
Singapore	54.8	42.0	54.2	76.2
Sweden	73.4	68.0	73.3	82.5
Switzerland	73.3	71.3	67.9	84.1
UK	64.8	68.1	46.5	85.0
USA	59.0	58.3	58.4	61.1
<b>Average</b>	<b>61.0</b>	<b>62.2</b>	<b>52.1</b>	<b>71.5</b>

Mercer (2012), *Melbourne Mercer Global Pension Index*, Australian Centre for Financial Studies, Melbourne

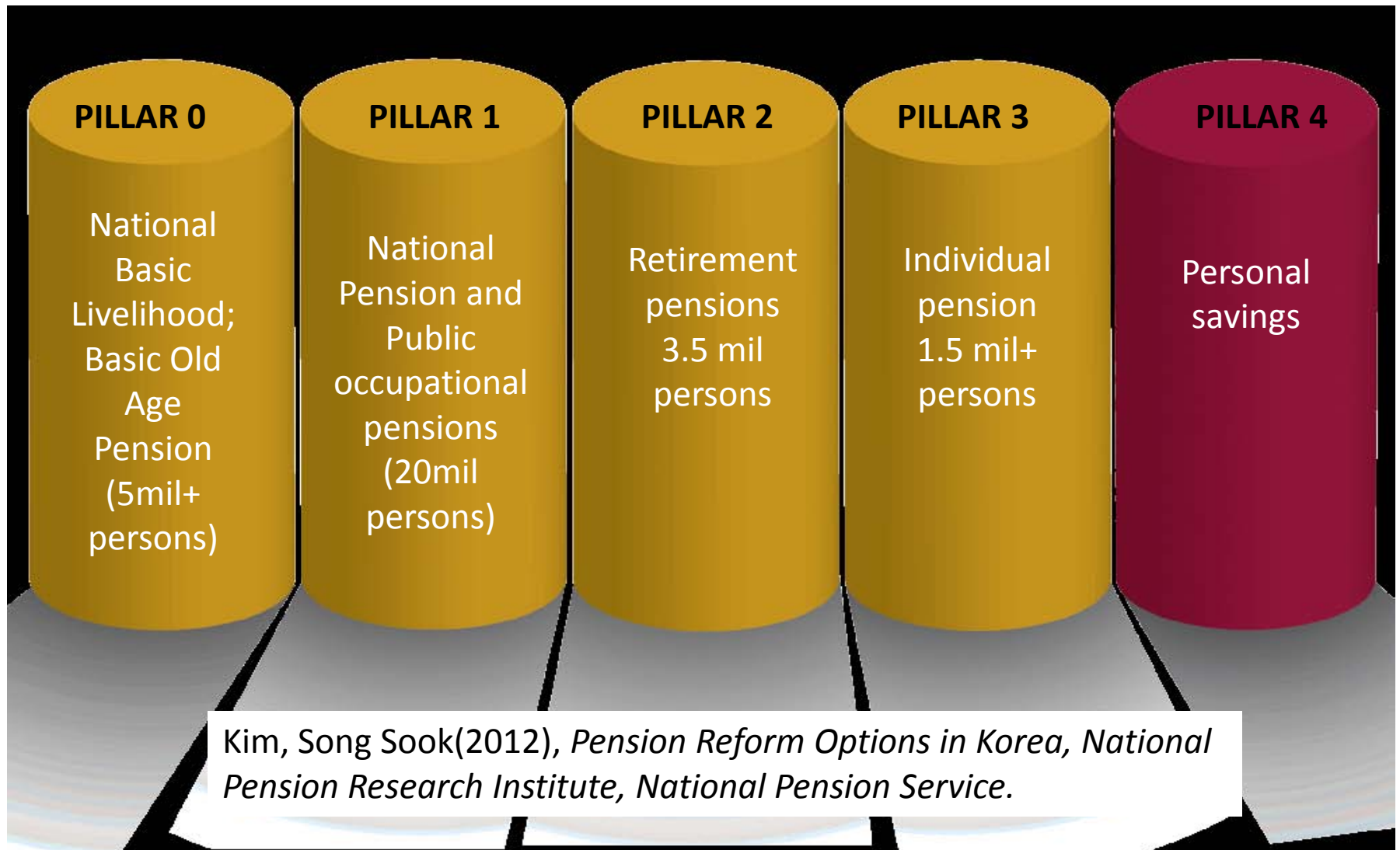
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# **STRUCTURAL OVERVIEW**

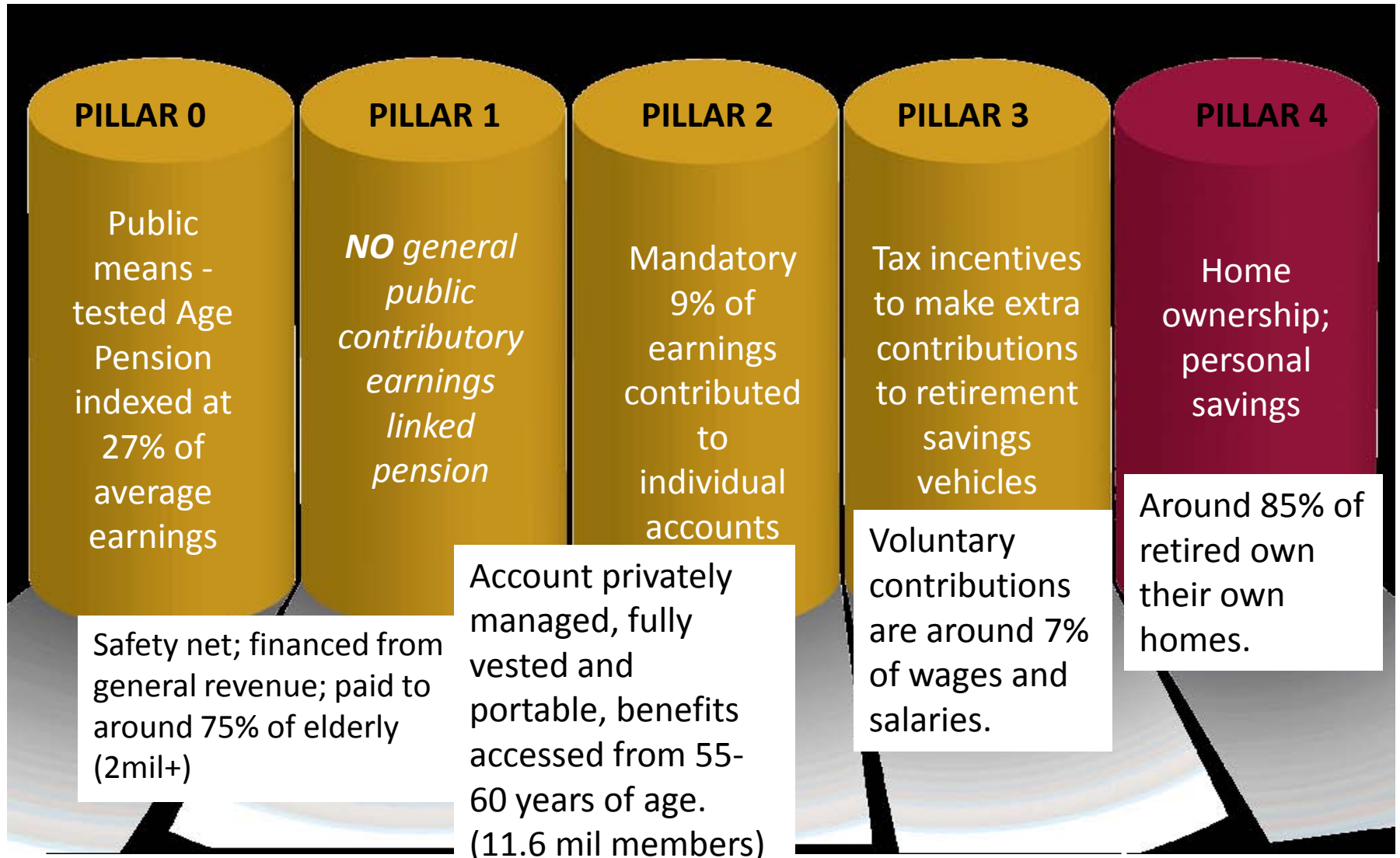
# World bank four pillar categorisation of retirement savings systems



# Korean retirement savings system



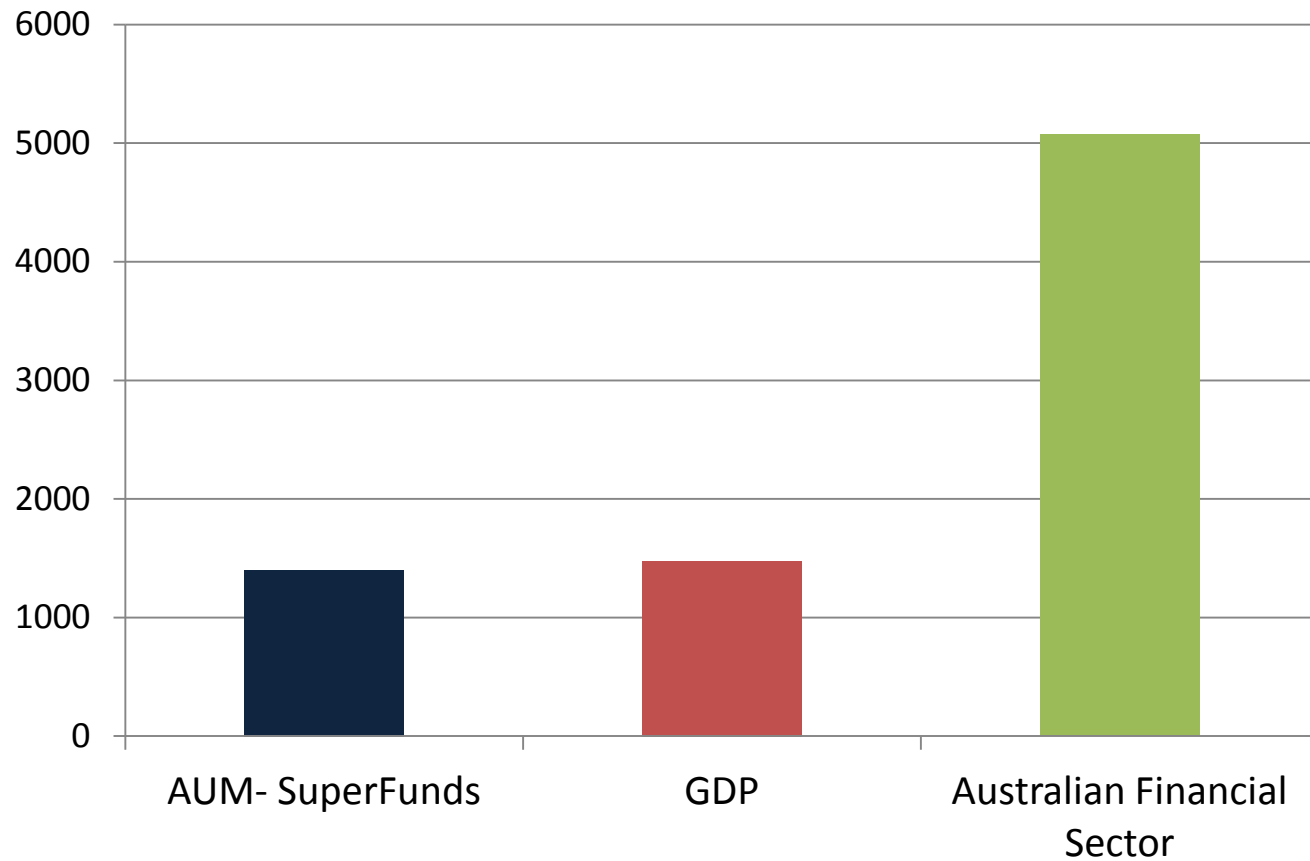
# Australian retirement savings system



# Australian retirement incomes system is large and growing rapidly.

- Sectoral **total assets \$1.46 trillion** at Sep 2012
  - Approximately 100% GDP
  - Large fund assets **\$834 billion**
  - Small (self-managed) fund assets **\$439 billion**
  - Public sector funds and life offices **\$128 billion**
- **Projected assets \$3 tr** by 2025; **\$6 tr** by 2036
- **Coverage** of employees: **96%** full time, **80%** part time, **73%** casual & self employed; around 11.6 million members

## Asset Under Management \$ (billion)



# **‘Superannuation Guarantee’ mandates contributions at 9% of earnings for employees.**

- Current contribution rate 9% of earnings **\$118b in 2012**
  - Superannuation phased in from 3% in 1992 to 9% in 2003
  - Rising to 12% from 2013 – 2020
- Employers contribute for employees **\$82b**
- Employees may contribute for themselves **\$36b**
- Must be made to a **complying (regulated)** Superannuation Fund or Retirement Savings Account. **31.9million accounts**  
**2.7 ac'ts/member**
- Most are defined contribution, individual accounts
- Members may choose Fund or default to employer's choice, but few make a choice
- ***Employers who fail to pay are penalised by Tax Office***

# Superannuation Guarantee operates through a concessional taxation structure (TTE).

- Employer **contributions** *tax deductible* to employer and taxed at **15%** in hands of superannuation
- Employee **contributions** out of after tax income-**not taxed** in hands of superannuation fund
- Fund earnings – taxed at **15%** (except Capital Gains at 10 or 15%), imputation credits (**effective rate around 7-8%**)
- Benefits (**not taxed** after age 60)

[Note – concessional and non-concessional contributions are capped. Excess contributions tax applies 31.5% for concessional contributions, 46.5% for non-concessional contributions]

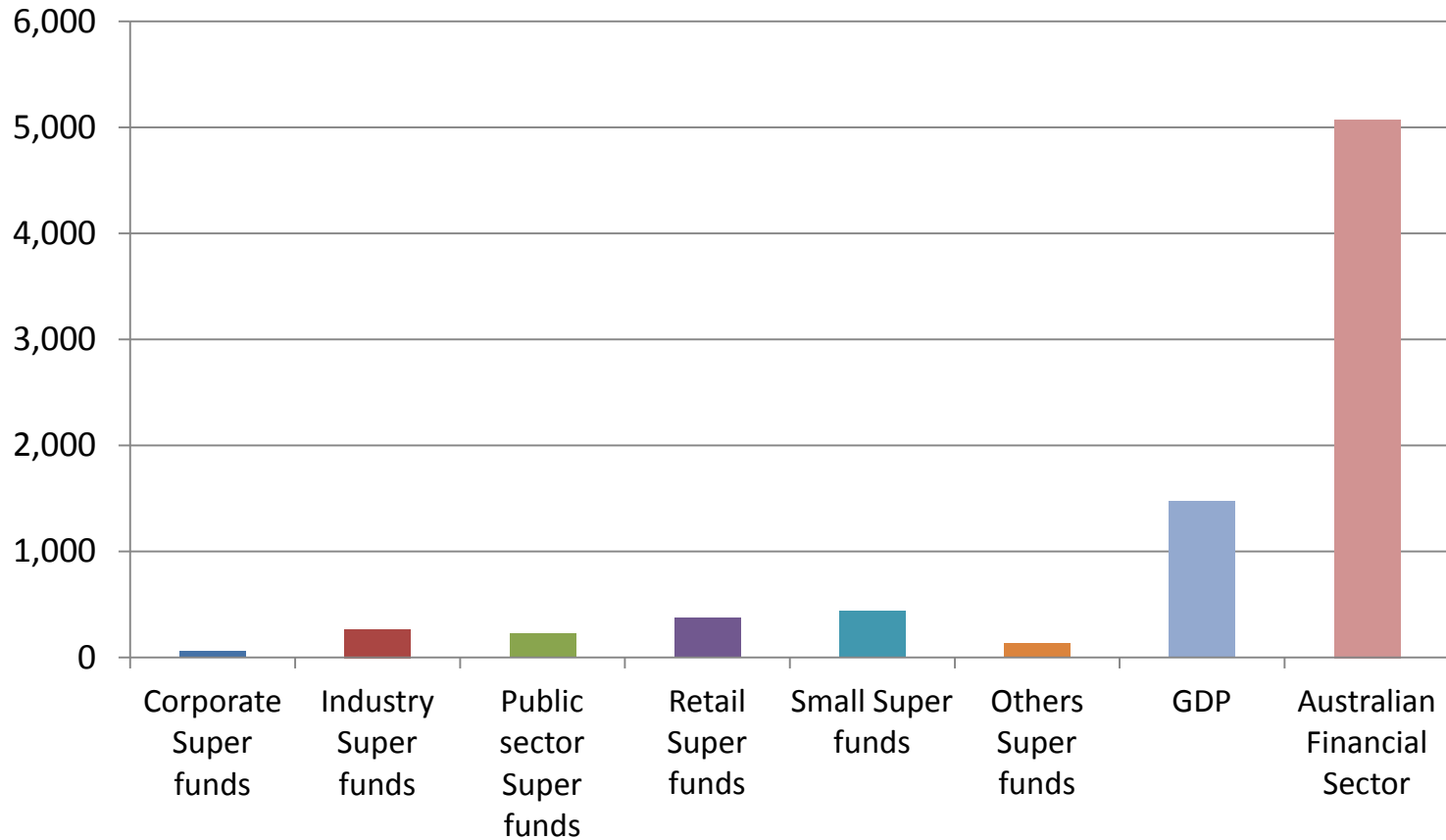
# There are six types of complying superannuation funds.

- **‘Sole purpose’ of all funds is to provide retirement benefits**
- **Not-for-profit superannuation funds**
  - Corporate funds (*employer-sponsored, often DB, not public offer, equal representation trustees*)
  - Industry fund (*multi-employer, DC, public offer, equal representation trustees*)
  - Public sector fund (federal or state government established, DB/DC)
- **For-profit superannuation funds**
  - Retail fund (*banks and life insurers, public offer, DC, corporate trustees*)
- **Small superannuation funds**
  - Small APRA funds
  - Self managed superannuation funds (SMSF) (*<5 trustee-members, not public offer, DC*)

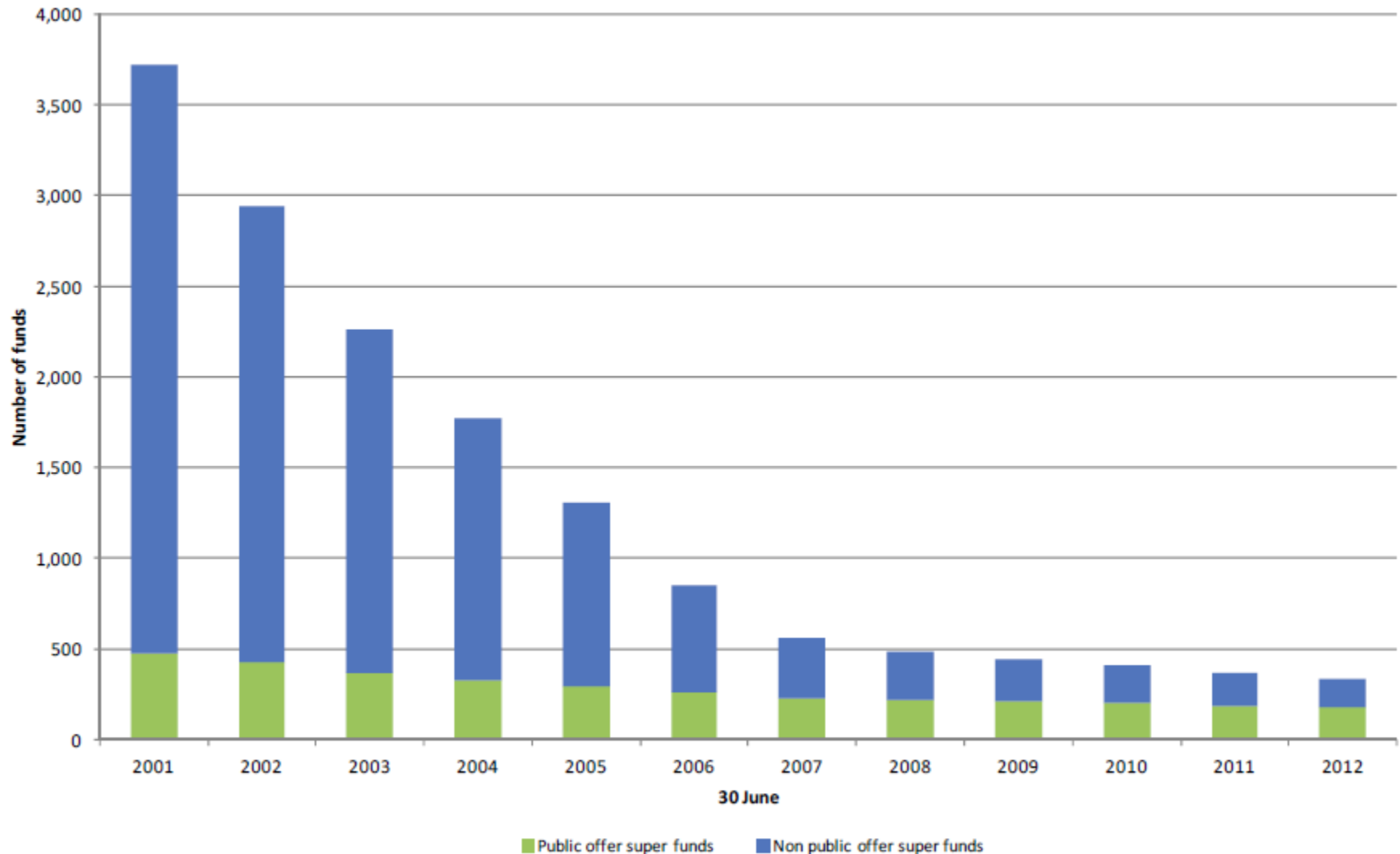
# Characteristics of superannuation funds – by functional classification, June 2012.

	No. funds	No. accounts '000	Av. Ac't balance \$000	Assets, \$ bill
Corporate	122	551	101.8	56.1
Industry	56	11,664	22.9	267.3
Public Sector	39	3,371	66.1	222.7
Retail	135	15,408	24.1	371.4
Small APRA	3,201	918	480.4	1.8
Self managed superannuation fund - SMSF	478,263			439.1
Other	141			129.8
Total	481,957	31,911		1,400

## Asset Under Management \$ (billion)



# The number of large funds has continued to fall but concentration is still low.

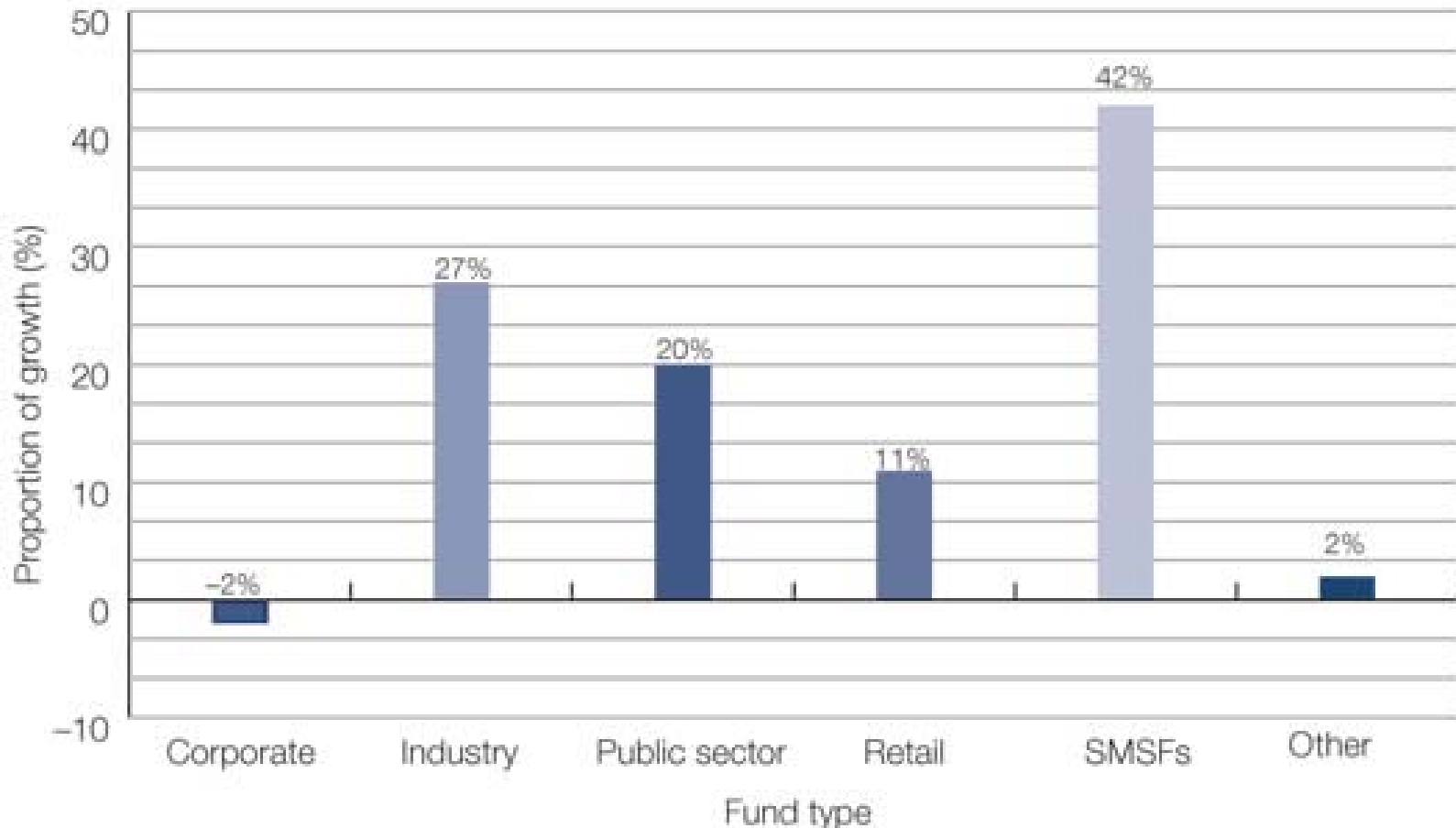


<sup>a</sup>excludes small funds and pooled superannuation trusts

Source: APRA Annual Superannuation Bulletin June 2012

# Self-managed sector grows rapidly at the expense of large funds.

Proportion of 2008 to 2012 total superannuation asset growth by fund type



Source: Australian Tax Office (2013) Self-managed super funds: A statistical overview 2010-11. Canberra, ACT.

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# **INVESTMENT**

# **Fund trustees are responsible for an investment strategy for members' savings.**

Strategy must consider:

- Risk and likely return
- Diversification through the whole portfolio
- Liquidity
- Liabilities

Borrowing and 'in-house' asset holdings are not allowed.

Alternative investments (private equity, infrastructure, PPPs etc) allowed if portfolio is well-diversified.

# Members are offered a choice from a menu of investment options.

## Choices of investment option

- *Not-for-profit* (corporate, industry, public sector)
  - average 7-10 options: multi manager diversified (growth, conservative etc...)
- *For profit*
  - average 257 options: Single and multi manager, specialised and diversified, individual equities
- *Self managed* – unlimited
- If no choice – contributions placed in *default option* (43% of assets)
- **Average asset allocation of default investment option**
  - **28% Aust shares, 23% Int'l shares, 10% property, 9% Aust fixed interest, 5% Int'l fixed interest, 9% cash, 13% other**

# Asset allocation of large and self-managed funds, June 2012.

Asset class	Large funds %	Self managed funds%
Cash and short term deposits		27
Fixed Interest		11
Australian Shares		36
International Shares	22	8
Property		18
Other (Hedge funds, agricultural funds, geared and ungeared trusts)	16	1

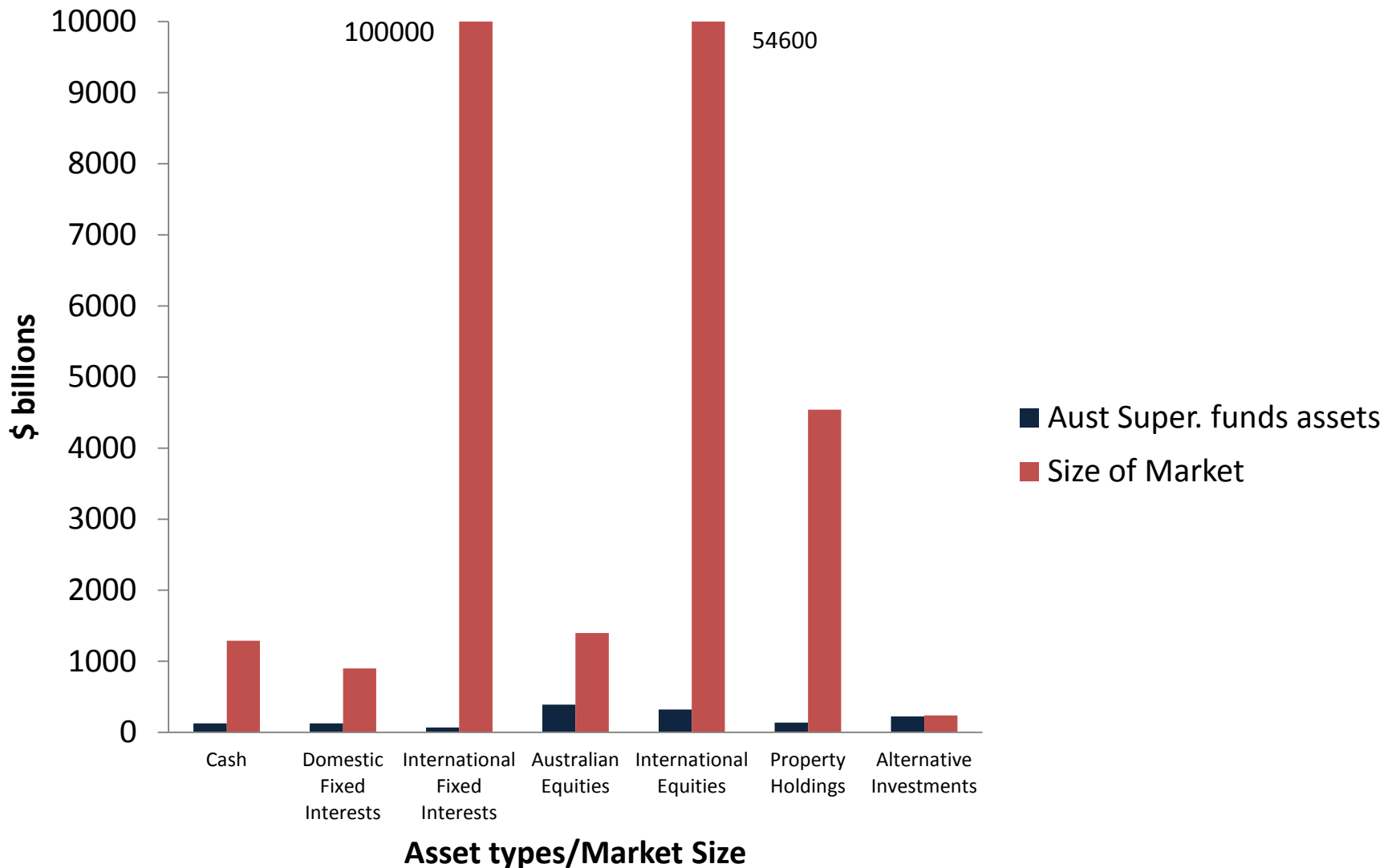
The Top 10 shares in the ASX make up 17.9% of total SMSF assets, nearly 49% of all the Australian Equity allocation.

Managed funds and EFTs more popular, tilt towards Asia and emerging markets.

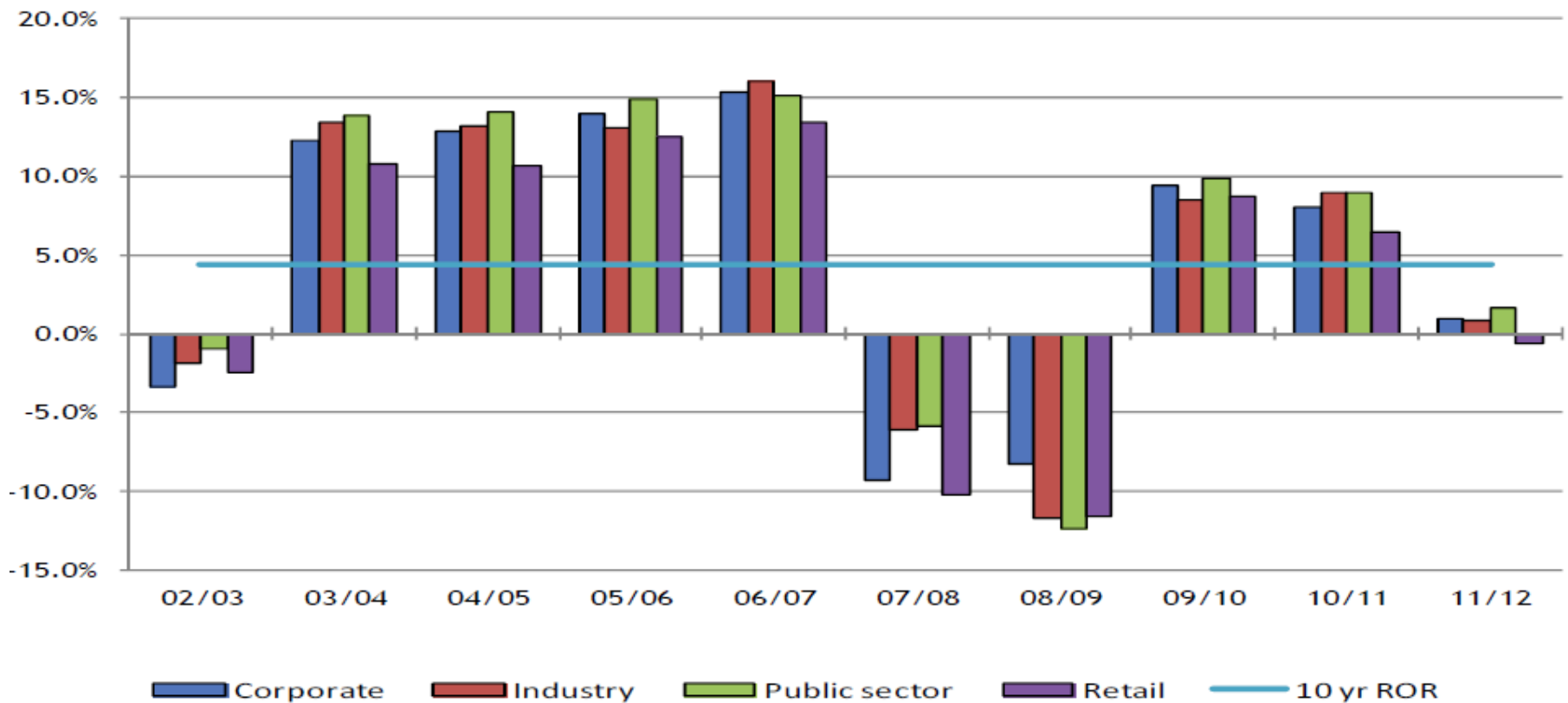
Direct property is 16% and listed is 2%, mainly residential.

Source: APRA Annual Superannuation Bulletin June 2012; Multiport Pty Ltd

## Relative size of Superannuation fund investment to market



# Real rate of return has averaged 2-2.5% p.a. over 10 years.



Source: APRA Annual Superannuation Bulletin June 2012

# Costs and charges differ across different sectors of the superannuation industry and affect ROR.

## Fees and charges (voluntary and SG)

- Differs by fund type. eg (total operating expense + investment expense)/assets 2011
  - Industry fund: 0.74% assets
  - Public sector fund: 0.45% assets
  - Retail fund: 0.85% assets

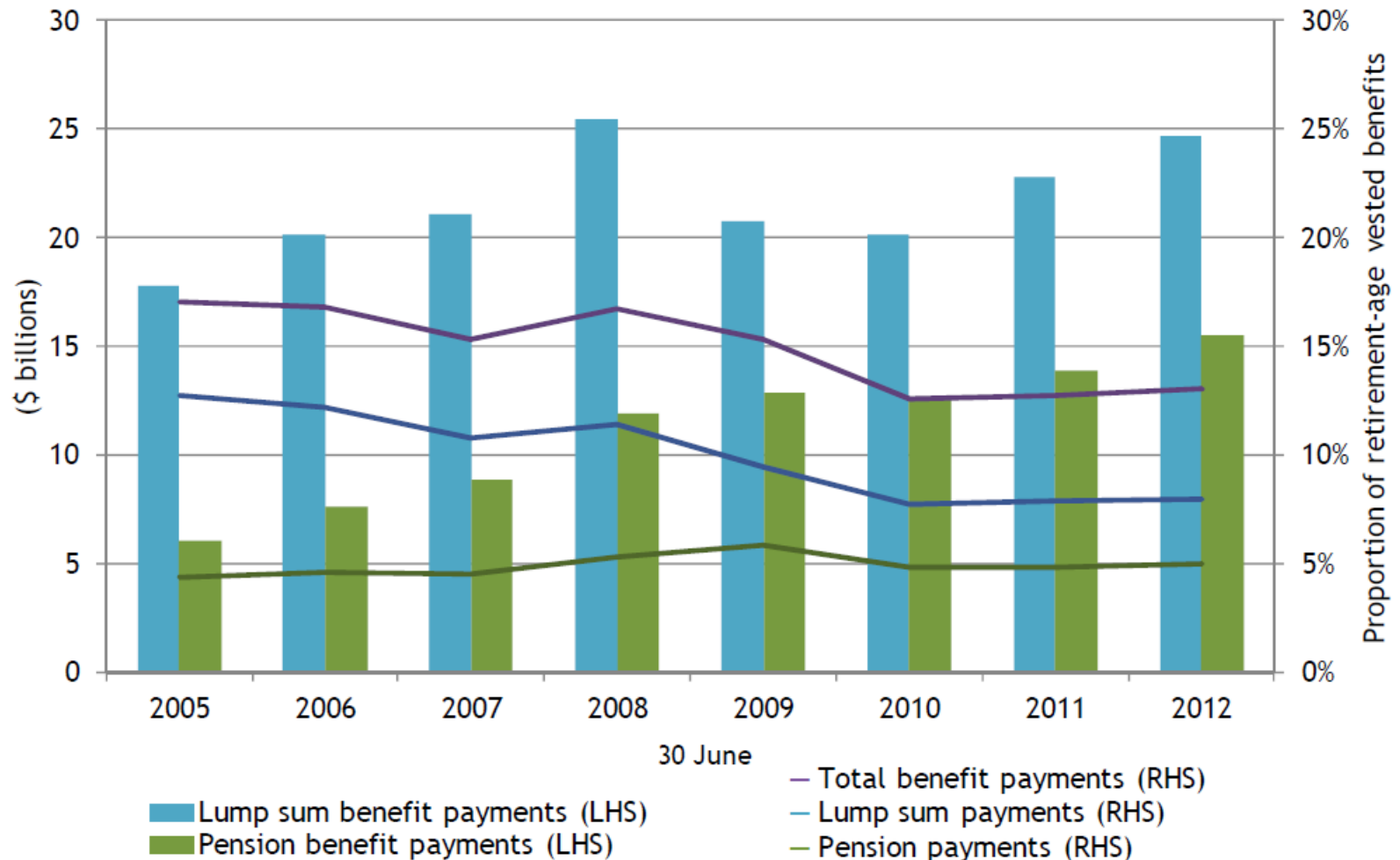
## Net performance (voluntary and SG)

- Differs by fund type. e.g. Rate of return 2002-2011
  - Industry fund: 4.9%
  - Public sector fund: 5.2%
  - Retail fund: 3.3%

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# **BENEFITS AND ADEQUACY**

# Benefits can be taken as a lump sum or as an income stream but annuitisation is very low.



<sup>a</sup> Excludes exempt public sector superannuation schemes, small funds and eligible rollover funds

# Projected replacement rates for full working life are good for median income employees.

Income	Projected replacement rate	Proportion of retirement income from superannuation	Proportion of maximum age pension
Median income	77.7%	37.3%	94.5%
AWOTE	67.2%	46.0%	88.8%
1.5 AWOTE	55.4%	60.0%	76.5%
2.5 AWOTE	47.0%	76.5%	55.2%

Source: RIM Group, Australian Treasury, Canberra

# Assessing superannuation –How well does Australia’s superannuation system address retirement risks?

<b>Retirement risk</b>	<b>Superannuation</b>
<b>Replacement risk</b>	Depends: on contribution rate, wages and wages growth, duration of contributions (labour force participation), tax on contributions, administrative fees, choice of superannuation fund, asset allocation (investment choice), investment fees, taxes on fund earnings, benefit type (asset allocation, admin and investment fees), tax on benefits (currently tax free), life expectancy, eligibility for public Age Pension
<b>Investment risk</b>	<b>No: Defined contributions (DC), benefit choice allows exposure to market risk in retirement</b>
<b>Longevity risk</b>	<b>No: no requirement to take retirement benefits with longevity features</b>
<b>Inflation risk</b>	<b>No: no requirement to take ‘indexed’ retirement benefits</b>
<b>Annuity risk</b>	<b>Na</b>
<b>Contingency risk</b>	<b>Yes</b>
<b>Default risk</b>	<b>Well regulated industry</b>
<b>Political risk</b>	<b>Most probably yes</b>

## **Current and future challenges.**

- Rapid growth of contributions creates investment challenges
- Rapid regulatory change creates compliance challenges
- Potential for regulatory risk over tax structures
- Large outflows to self-managed sector
- Increasing number of retirees needing retirement income products