

Super – An Australia – New Zealand Point of View

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Address to Brook Breakfast, Rotorua, NZ

27 July 2007

I am delighted to be here today and I thank my generous hosts for inviting me.

I have a high regard for the way in which you do business on this side of the Tasman, and I also have a high regard for a quite

a number of things that you have created in this great nation called New Zealand. You are a nation renowned for both resourcefulness and inventiveness...so it is indeed a privilege to be here this morning.

One of my connections with New Zealand has been via my interest in military history. Last year I visited Chunak Bair in Gallipoli...and there I saw first hand, the terrain that your forefathers ascended in 1915 in order to take hold of that vital piece of land in Turkey that overlooks the Dardenelles...what great courage and tenacity they showed. The Les Carylton book on *Gallipoli* was my main source for this story. It also refers to the great regiments which were formed out of the NZ provinces, and the characters who led the charge for New Zealand to become a nation in its own right.

Last year I also read the book by Rick Atkinson titled *An army at dawn*.....this contains a gripping account of the NZ Division in Tunisia in April-May 1943 under the leadership of the crusty

General Freyberg. The great British General, Brian Horrocks, described the NZ effort as the ‘most gallant feat of arms I witnessed in a war’. But this came at the price of 459 men and 34 officers.’

But today I am here today to talk about another battle...the battle to develop the best public policy to meet the needs of New Zealanders in retirement. This has been a battle royale. I understand...it has been a battle which can trace its beginnings to 20 or more years ago.,it has ebbed and flowed, and now post, 1 July 2007 the world will witness New Zealand adopting a quality, almost universal, retirement savings system.

Your public policy officials and elected representatives and ministers have done a superb job in marshalling the demographic, market and investment data to produce a preferred policy outcome, now known as the KiwiSaver scheme.

I would also like to mention that the industry association ISI has played a catalytic role, and in this regard my colleague Vance Arkininstall has kept me briefed on progress.

Your KiwiSaver scheme has a solid contributions base, it has a neatly arranged optional structure of either four or eight per cent and it gives the employee and his/her employer the additional option of contributing further pre tax dollars into a Kiwi Saver account. It is worth remembering that from little things, big things grow and that Australia began with a contribution rate of just 3%.

As you begin to think about the role that financial advice might play in the new regime it is instructive to cover some the issues that have played out in the Australian market since the introduction of our universal pension scheme.

Internationally, now, Australia and New Zealand share more than a great rugby tradition....they are now seen as two prime

and recent examples of nations that have gritted their teeth and made mega decisions on the way forward for private pensions policy.

Our joint strength is grounded in a number of key features of our respective systems, viz:

- We both have target contribution levels designed to produce certain retirement savings outcomes;
- We both funnel moneys from the workplace into retirement savings accounts facilitated by the private sector within a competitive market place;
- Both countries are endeavouring to address the demographic and longevity imperatives that will place great stress on the public pension system; and

- Advice can and will play a critical role in determining the overall effectiveness of the system.

But as our universal system of retirement savings was implemented, albeit somewhat earlier than KiwiSaver, and as I was asked to cover this in today's address, I would like to point out some of the lessons learned under our Superannuation Guarantee.

The first learning is that you have a much more imaginative and branded name. KiwiSaver presses all of the right buttons with consumers, the media and the world.

The second learning is that no matter how one looks at this KiwiSaver policy, the industry has inherited a community service obligation- and with a CSO goes a number of critical responsibilities.

Customers should be treated with the utmost of priority. This will no doubt be manifested in the requirements of the laws which underpin disclosure and licensing. Product providers and advisers alike will also have an obligation to behave ethically and in accordance with best industry practice – so I will be interested to observe your work on the self- regulation front.

The third learning is that you need an effective customer disputes resolution system.

We in Australia have two bodies, one is a Government sponsored entity (The Superannuation Complaints Tribunal) which resolves disputes between the superannuation funds and their members.

The other is the Finance Industry Complaints Service. The following two slides [**Slide 1 and Slide 2**] show the extent of disputation in Australia. You will notice that the industry and superannuation fund trustees have gone to great lengths to keep

the number of disputes to a minimum. Also, you will notice that disputes on advice are low, given that there are some 26 million accounts estimated to be in existence in Australia (check)

Let me now show some slides [**Slide 3 and Slide 4**] on disputes in the UK and the USA. These slides show much greater numbers of disputes.

I am advised that the NZ Government is working on a dispute resolution scheme and I encourage the industry to embrace these proposals in a spirit of openness and cooperation - as a sound dispute resolution mechanism should be an asset which gives your industry a winning formula which will inspire investor confidence.

The fourth learning is that the industry should track customer sentiment on a range of concerns. Things like the quality of advice, the quality of investor materials, the level of fees and the reputation of the industry all need to be surveyed regularly.

These results should be responded to by the industry and it should be prepared to share these results with the community and government. I guess my message is: disclose, disclose, disclose, whether or not the results are to your liking. If they show you have to do better as an industry, say so, fix the problem and move on.

If you do not track your consumer success you will allow the opponents of KiwiSaver to fill the vacuum, possibly with less reliable and less valid data. This will undermine the system and in no way encourage the body politic to enhance it.

The following slide shows some of the customer sentiment data.

[Slide 5]

As you can see from this data we have made great strides under our financial services regulation to deliver better customer outcomes. We have delivered significantly better outcomes on advice, product trust and safety, fees and charges, and overall on a range of 13 indicators we have moved our industry score from 6.3 to 7.4 over an 18 month period.

We plan to release more consumer data as part of the industry's disclosure project which will have an initial airing at IFSA's Annual Conference next week. We embarked on this project because the IFSA membership acknowledges that still more can be done. In this regard the length of our prospectus and advice documents is unwieldy and in need of compaction.

The fifth learning is that good financial advice should be one of the system's critical underpinnings.

It might seem at first blush that the KiwiSaver policy presents very limited opportunities for advisers to engage with the full

gamut of customers. The possible caps on fees and the somewhat limited subsidy support for flat fee advice could be seen as limiting factors.

It is important to keep the main game in mind here.

As with all government policies the KiwiSaver policy will have what I call a 'headline effect' and a 'cascade impact'.

It is easy to quantify the dollar flows from the 4 plus 4 plus arrangements. It will be possible to estimate the level of voluntary savings. Some estimates will be made too, on what flows of ordinary savings will be into the new KiwiSaver accounts.

What is difficult to measure is the overall impact on community attitudes to savings versus other lifestyle choices and other assets both financial and property-related. If Australian experience is a guide, in the absence of other tax preferred

savings vehicles, within the medium term, my expectation is that the KiwiSaver will become the preferred saving and investment vehicle.

In this regard the following chart [**slide 6**] shows how over 15 years managed funds in Australia have evolved from being just under 55 per cent to 110 per cent of GDP.

This outcome has been driven by two forces – the first is the move to voluntary contributions and the second has been driven by successive Government decisions to give further ‘boost’ incentives and also to remove significant disincentives. In other words, from a baseline nine per cent compulsion or headline effect, we have had a number of ‘cascade’ outcomes. The political imperative to enhance the system will come if the industry plays its part in laying down the strongest of foundations.

And when balances become significant, advice will be needed and needed in spades. Indications in Australia are that people really start to take an interest and engage with their retirement savings when they hit around \$50,000.

Currently, in Australia we have an advice shortage. Especially in the boom resources state, Western Australia, where there has been only a modest expansion in numbers of advisers but with massive increases in private wealth. The demand for financial planning has exploded. Our members are finding it exceedingly difficult to lure people from the highly paid resource sector.

In other states the situation is not as dire but it remains problematic and shows no signs of easing.

Seek.com.au data for the last thirty days (July 2007) shows that there are currently 5200 jobs in financial planning firms, and this number has increased four fold since my last visit to seek in February when the number was 1300.

So my entreaty is start planning the ways and means of offering scaleable and affordable advice with KiwiSaver – you might need to offer some loss leading services in the early years but in time the more profitable accounts will come.

Clearly in coming years there will be a virtually insatiable appetite for good advice.

My sixth learning concerns insurance. At about the same time that we introduced our SG system we removed the tax incentives for many life insurance products. Hence it became more attractive to offer life insurance as a bundled product within an SG accumulation fund. As well, this form of largely non-underwritten insurance became more affordable for middle and lower income earning Australians.

In Australia, paying for your life insurance out of pre-tax dollars and enjoying the cheaper premiums via group insurance in

superannuation is the preferred life insurance pathway. It is also possible to increase the level of cover within your super by buying extra units.

For instance, a 45-year-old male non-smoker on the top marginal tax rate of 46.5% can fund \$1 million death and TPD cover with an annual premium of \$1868 through super if he salary-sacrifices. If the premium were paid out of *post-tax* income, the cost would be \$3491.

However, the average 'group' death cover in industry funds tends to be in the vicinity of \$50,000 to \$70,000 -- nowhere near the 10 times annual salary that actuaries Rice Warner suggest is needed for those with dependent children in a 2005 study conducted for IFSA. With the average new mortgage in Australia weighing in at around \$235,000, people relying on the 'group' cover within their employer's default super fund are likely to leave their surviving family under enormous financial

strain if they were to die. And tragically, more than 4,400 people in Australia with children at home- *do* die each year, according to the ABS. For less than the price of a cup of coffee a day, we can make sure that those they leave behind can carry on financially.

Notwithstanding the fact that Australians are grossly underinsured, bundling insurance within a retirement savings product is good public policy, as in the long run it will assist families in the event of the death, illness or injury of a breadwinner.

Accordingly, I commend this method of risk protection to the KiwiSaver policymakers.

Finally, my seventh learning centres on the risk profile of a typical portfolio within the KiwiSaver system. We need to take a realistic view of the term of KiwiSaver accounts – put simply,

they will be for thirty or forty years - and beyond - once retirees begin taking income streams.

The premium for taking an investment risk is a proven feature of long term savings, and it is important that KiwiSavers access the equity markets that in the long term deliver superior returns.

In Australia a typical account has approximately 70 per cent in domestic and international equities and listed property stocks.

From a NZ perspective I note that your own NZ Super Fund has more than 70 per cent of its investments in growth assets, with the balance in cash and fixed interest.

Ladies and gentlemen.

I began my address with an allusion to New Zealand's 100 plus years of military history. I said that long term policy on savings is a battle - whether it is in New Zealand or in Australia.

It is a battle because Governments the world over set priorities according to their mandate and the election cycle is more like 3 or 4 years than 40 years. The average life of a Federal Government in Australia is 2.8 years and increasingly, governments are moving to almost continual campaign mode - which can leave limited time for 'deep thought' and policy development- although Australian governments of the same political persuasion typically serve at least two terms.

The Kiwisaver policy should be seen as the beginning of a new policy development cycle and if the industry delivers to both government and the community, expect new and even more attractive announcements on long term savings.

I thank you and wish you well in your endeavours.

