Measuring the success of superannuation against retirement incomes

The success of Australia's superannuation system is too often measured by its rapid growth to $3.4 trillion in savings, not by its actual objective, which is to provide income for Australians in retirement.

Over the next decade three million Australians will start drawing down their collective $1.5 trillion in superannuation savings and weaknesses in the design of what is otherwise a world-leading retirement system will be exposed.

New research by NMG Consulting for the Financial Services Council (FSC) has demonstrated that retirees are currently drawing down 17 per cent less income in their retirement from their superannuation than what is optimal.

Without reform to ensure that superannuation operates as efficiently as possible to raise retirees' living standards, the system will continue to be targeted by vested interests arguing for higher taxes on retirement savings.

The FSC research provides a road map to a more efficient system that would increase the annual benefits paid out of superannuation as retirement income by 10 per cent each year. Aggregate income paid to Australian retirees would be increased by $397 billion by 2050, without additional contributions to the system beyond the currently legislated move to 12 per cent.

It would halve the amount of superannuation savings left to future generations as bequests each year by 2060, removing a key inefficiency in the system that has become a lightning rod for superannuation's detractors.

The FSC road map will also ensure the superannuation system does all that can be expected of it to support a Federal Budget that is running a 2 per cent structural deficit over the medium-term, without the need for punitive and unfair new taxes.

The FSC road map is centred around action in three new areas:

- Encouraging innovative, new retirement income products to come to market, including a disclosure framework to allow consumers to compare retirement income products and a simplified process to modernise legacy products.
- Helping consumers see and use superannuation as primarily for spending during retirement, including making financial advice more affordable and amending disclosure rules to have a drawdown focus.
- Helping consumers take control of their superannuation by simplifying how it interacts with other parts of the retirement system, including the aged pension, aged care and health care.

One action the Government is already considering is ensuring Australians can access high-quality and affordable financial advice.

FSC analysis has shown that whilst Australian households are among the wealthiest in the world, far too many Australian consumers score poorly on measures of financial literacy, challenging the complex decisions they must make when they retire with considerable superannuation savings.

The Household, Income and Labour Dynamics in Australia (HILDA) 2016 survey data of financial literacy found that only 45 per cent of Australian adults are financially literate, based on testing understanding of three key concepts: interest rates, inflation and diversification.

The most recent 2020 HILDA survey suggests that Australia is going backwards against this measure, with the financial literacy gap between men and women, as well as older and younger Australians increasing.

NMG Consulting modelling demonstrates that implementing the Quality of Advice review will help Australians access the financial advice that will make retirement planning more efficient and result in 100,000 more retirees draw down an extra $10,000 each in increased retirement incomes every year.

Overall, by implementing the FSC road map, total superannuation system assets would be 12 per cent lower by 2060, or $1.6 trillion.

Counterintuitively for a peak industry body, the FSC is arguing to shrink the size of the superannuation pool over the long-term, which would have the effect of lowering total fees for the industry. A smaller industry would also receive less Government concessional tax benefits over time.

Delivering on the promise of the superannuation system to Australian retirees is where consumers' and the financial services industry's interests align, however, and the FSC proposes these reforms for the simple reason that they will deliver consumers higher standards of living in retirement.

With 800 Australians retiring every day over the next decade, if the Government fails to focus on improving the efficiency of the retirement system it will put the longer-term sustainability of the system at risk.

Australians work hard over their working lives to save for their own retirement, and we owe it to them to deliver policy settings that give them the confidence to enjoy the highest standard of living in retirement.

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