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ASFA
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AUSTRALIA'S FUTURE RETIREES

The Demography, Pathology, Sociology and Financial Position of Australia's Future Retirees

Discussion Paper

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1. The Demography of Australia's Future Retirees

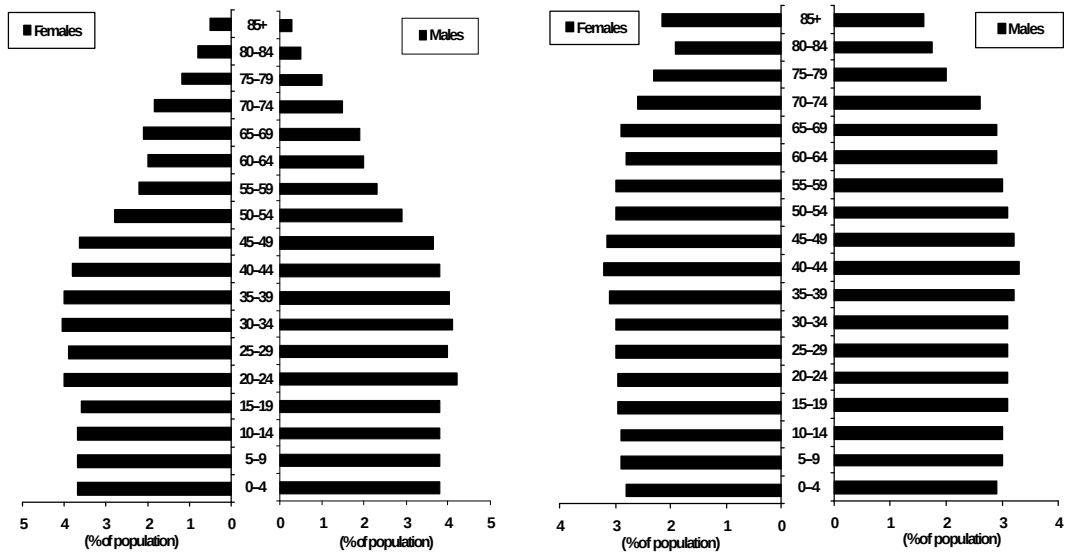
"Already there are more people aged over 65 on earth today than all the over-65's who have lived since humankind first existed."[1]

Traditionally, analysis of Australia's demographic direction has centred on the need to establish an ideal population size. The "populate or perish" policies implemented after World War II were based on perceptions of a population size too small to guarantee both security and the capitalisation of economic potential.

More recently however, the emphasis of concern has fallen strongly on the structural characteristics of Australia's population. Or more specifically, on its age profile. Australia's population structure is among the younger of the highly developed nations of the world, but like most developed countries, Australia is confronted with the social and economic consequences associated with a large and rapidly growing aged population. By the middle of next century the number of aged Australians is expected to double reaching approximately 5.5 million, or more than 20% of the entire population.

Fig 1 - Age-Sex Profile of Australia's Population

1995 (actual) *2041 (projected)*



source: ABS 1996.

1.1 An Ageing Population

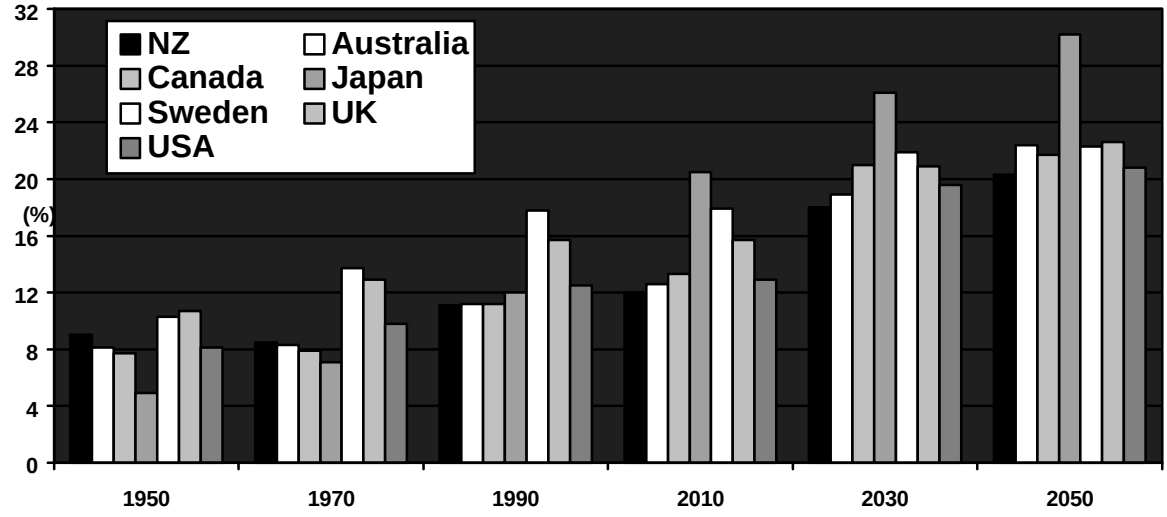
The world's population is ageing. Already there are more people aged over 65 on earth today than all the over-65s who have lived since humankind first existed. According to the World Health Organisation, 540 million (including 330 million in developing countries) of the world's 5.8 billion people are over the age of 60 and

[1] Parliament of Victoria, 1997

approximately 50 million are over the age of 80. By 2020, the number of older people in the world is set to double to about 1 billion.

In countries like Japan, Germany, New Zealand and Canada, as is the case in Australia, the proportion of the population aged over 65 is projected to double by the year 2050. Over the same time frame, the proportion of aged citizens in countries such as Indonesia, Singapore, Malaysia, Vietnam and Papua New Guinea is expected to triple.

Fig 2 - Population aged 65 Years and Over as a Percentage of the Total Population



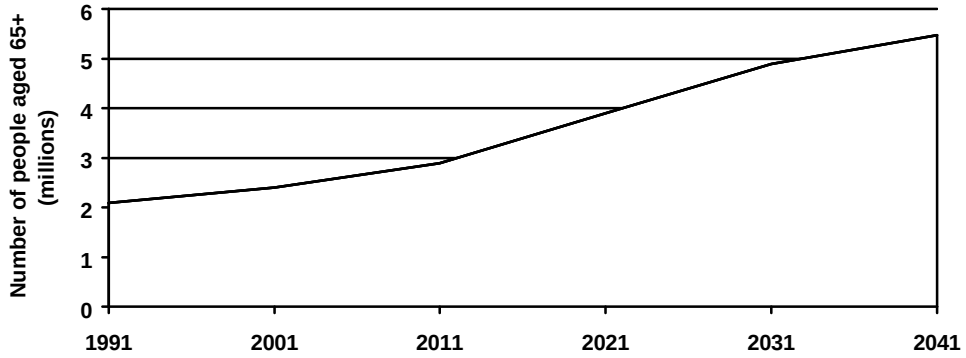
source: World Population Projections, 1994 Revisions, United Nations

1.2 Ageing in Australia

The phenomenon of demographic ageing is not new to Australia. Since 1861, when only 1% of Australia's population was over the age of 65, Australian society has witnessed a progressive ageing in the make-up of its citizens. By the turn of the century, when the total population of Australia was less than 4 million, the proportion of Australians over the age of 65 had increased to 4%. In the late 1970s, this figure had risen to 9% (1.3 million people) and over the 1990s, when the Australian population as a whole has grown by 12%, the proportion of the population over the age of 65 grew by 22% to total in excess of 2 million people (12% of total population).

Current projections strongly suggest that the ageing of Australia's population will continue. The ABS (1996) projects that the number of persons aged 65 and over will rise from 2.1 million (12% of total population) in 1991 to 2.9 million (13.8%) in 2011, to 4.9 million (20.3%) by 2031 and to 5.47 million by 2041 (see Fig 3 below). The highest annual rates of growth in the proportion of the aged population are expected to occur between 2011 and 2021 as the cycle of baby boomers moving into their retirement years reaches its peak. These projections of the over 65 population are not very sensitive to changes in assumptions about immigration and fertility. However, overall population numbers would be affected by factors such as a large increase in immigration.

Fig 3 - Projected Increase in Population Aged 65+ Years

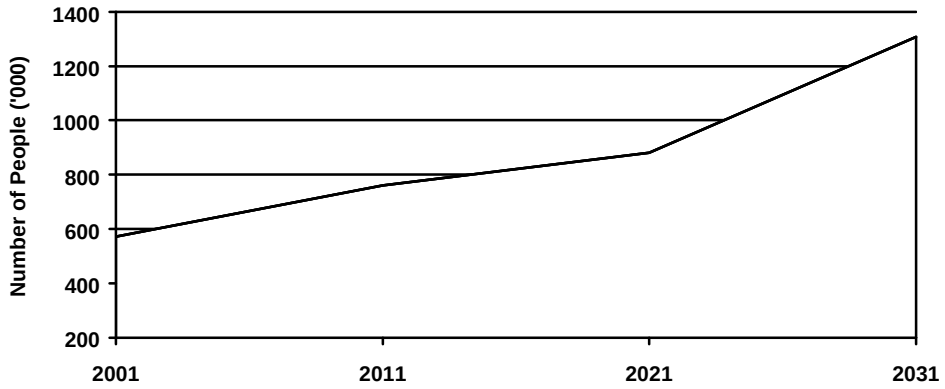


source: Parliament of Victoria 1997

1.2.1 Ageing of the Aged Population

The ABS (1997) also predicts a considerable increase in the number of 'old Australian population is not only ageing, but also getting relatively older. The number of people over the age of 80 is projected to increase faster than any other cohort of the aged population over the next decade and a half. The population of over 80s grew from 218,000 in 1976 to 485,000 in 1996 and is expected to grow to 760,000 (3.6% of total population) by 2011 and to 1.3 million by 2031 (5.5%). The number of those aged over 85 is also expected to increase, rising from 190,000 in 1995 to 470,000 in 2021 and reaching 1.3 million in 2051. By then, the median age of Australians is expected to be about 43 years (up from 34 in 1996), with the average life expectancy of males rising to 81 years and the average life expectancy of females to 86 years.

Fig 4 - Projected Increase in Population Aged 80+ Years



Source: Parliament of Victoria 1997

2. The Economics of Ageing

"In Australia, each aged person costs all Governments 2.3 times the cost of a young person. For the commonwealth Government the ratio is 4.1. Therefore in Australia the ageing of the population will significantly increase costs to governments, with the Commonwealth needing to substantially increase outlays."[2]

Much has been achieved with Australia's retirement income system in the last two decades. Major steps have been taken towards ensuring that Australians have access to a decent retirement income, increasing our national savings and getting ready for the ageing of our demographic structure.

However, the urgency with which the issues associated with demographic ageing will need to continually be addressed cannot be underestimated. The 'baby boom" generation will begin to impact considerably on retirement income expenditure in the next decade or so and have simultaneous demands for increasingly sophisticated medical care as they seek longer and better quality lives. The baby boom generation will be a powerful political force and how, not whether these provisions will be funded is the issue.

2.1 Intergenerational Equity - An Issue of Dependency

Recognition of the extent of forecast greying of the Australian population has fostered widespread and far reaching debate about the approach to the social programs and incentives which accommodate the population based on age related criteria. Much of the debate, particularly among policymakers, has centred on the ability of a proportionally smaller number of labour market participants to finance provisions for an increasingly large older population.

Many analysts have even predicted intergenerational resentment as those in the workforce today discover that they are paying not only for their own retirement, but also for that of those who have already retired.

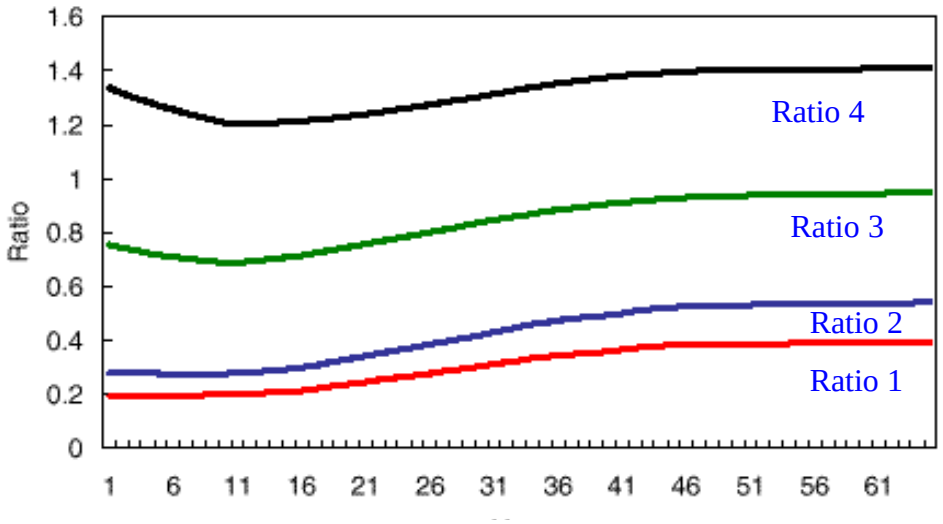
At this stage though, the issue of intergenerational equity does not appear to have infiltrated the wider social psyche, with the majority of Australians remaining strongly in favour of public support for retirement income. However, the situation may change, particularly if an increasingly politically relevant older population lobbies for greater intergenerational transfers.

2.1.1 Dependency Ratios

Dependency ratios are the most commonly employed economic measure used to define the level of dependence of one group in society to another. Simply, traditional dependency ratios are based on the premise that as a greater proportion of the population enters retirement, fewer active workers are left to support them. As a result, the cost to those in the labour force, and to the economy as a whole, becomes greater. However, it should be noted that any comprehensive analysis of dependency would also need to take into account the role of capital and capital ownership, including income derived from overseas investments.

[2] Gallagher 1995

Fig 5 - Projection of Dependency Ratios



Ratio 1: Ratio 65+ to 18-64
Ratio 2: Ratio pop 65+/all workers
Ratio 3: Ratio pop 65+ and not working/all workers
Ratio 4: Ratio of not working/all working

Source: Rothman 1998

The first projection of dependency in the above graph compares those of labour force age (18-64) with those over the age of 65 to produce the standard age dependency ratio. According to the Retirement Income Modelling Unit's projections, the standard age dependency ratio will rise from 0.19 in 1994-95 to 0.2 in 2005-6, 0.3 in 2024-25 and to 0.39 in 2059-60 - indicating a substantially increased fiscal responsibility on those of working age, particularly given the high relative cost that aged services represent to government.

The second ratio, although similar to the first, differs in that it excludes the assumption that labour force participation is uniform across all individuals in the 18-64 age group. This ratio compares those aged over 65 to the number of people actually working, and therefore presents a more useful projection of dependency. RIM analysis indicates that this ratio will fall slightly below the 0.28 level of 1994-95 until 2006, reflecting projected increases in labour force participation. The ratio is then expected to rise to 0.42 in 2024-25 and 0.54 in 2059-60.

RIM also projects :

- the ratio of all those not working and those over the age of 65 to the number of actual workers - the ratio moves from its current value of about 0.77 to 0.69 in 2005, to 0.84 in 2024-25 and to 0.95 in 2059-60.

- the ratio of all those not working to all those working - the ratio moves from its current value of about 1.36 to 1.2 in 2005, to 1.3 in 2024-25 and then to 1.4 in 2059-60.

2.2 Age Pension and Health Care Costs

2.2.1 Age Pension Costs

Department of Social Security statistics indicate that approximately 75% of Australians aged over 65 rely on either a full or part pension as part of their retirement income, costing the government $13.4 billion in 1997/98. Including income support for war veterans and their dependants raises the total to $17.8 billion.

From the data below, it is apparent that expenditure on age and veterans pensions will rise over time. The question of course is, what magnitude of rise indicates a threat to the long term sustainability of income provision for the aged. According to RIM projections (Rothman 1998) the risks associated with ensuring the affordability of future age and veteran pension costs depend largely on the probability of various policy scenarios.

Table 1 - Projected Cost of Age and Veterans Pensions as % of GDP - Various Scenarios

Year	Base	Without SG	Universal Pension	30% Pension
1998-99	2.99	2.99	3.68	2.99
1999-2000	2.94	2.94	3.61	3.45
2000-2001	2.94	2.94	3.62	3.45
2010-2011	3.06	3.08	3.81	3.61
2020-2021	3.55	3.67	4.72	4.22
2030-2031	4.07	4.33	5.79	4.86
2040-2041	4.49	4.76	6.38	5.33
2049-2050	4.48	4.76	6.44	5.32

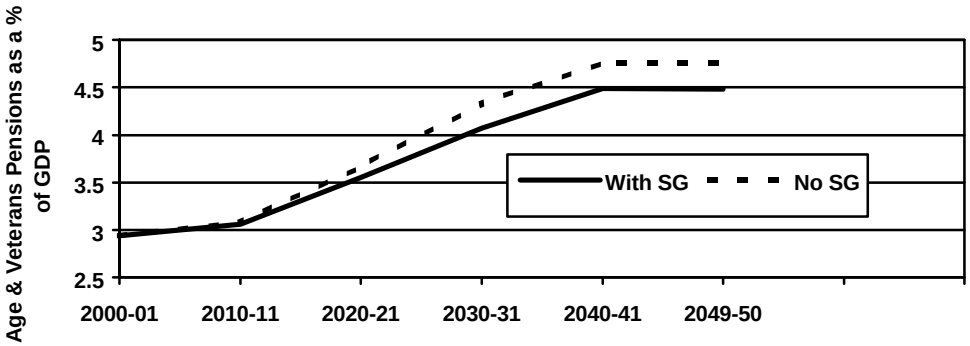
Source: Rothman 1998

Based on RIM analysis:

- the base case (defined as *"the continuation of voluntary superannuation saving and the Superannuation Guarantee (SG), with pensions indexed to AWOTE, but with threshold levels for income and assets tests indexed to CPI[3]"),* produces an increase in the cost of pensions as a % of GDP of 1.5% (to 4.48%) by 2050, which may well constitute a manageable increase in social expenditure. If, however, the SG policy had not been introduced, then government outlays on pensions would have increased by a further 0.28% of GDP (or about $1.5 billion in current terms) to 4.76% of GDP by 2050;

[3] Rothman 1998

Fig 6 - Projection of The Effect of the SG on Age & Veterans Pensions Outlays



Data source : Rothman 1998

- the universal pension scenario, where pension costs are projected to exceed the current base case by 3.5% of GDP in the long term, will more than likely imply an unsustainably large fiscal outlay;

- the scenario where the full age pension rises from its current benchmark of 25% of average male wages to 30%, resulting in a rise in pension outlays of about 2.3% of GDP above the current base in the long term, could also be considered prohibitively costly.

Other issues will also impact on the future cost of aged and veterans pensions costs. The combined effect of factors such as the level of dissipation of lifetime savings, the rate of drawdown of the capital component of investments, changing patterns of retirement over time, alterations to deeming rate policy and the investment patterns and mix employed by typical retirees represent a risk on the upward side of about 10% (or 0.35% of GDP) of pension costs in 2019-2020 according to RIM (Rothman).

2.2.2 Health Care Costs

Potentially, the fiscal risk associated with the level of government spending required to fund health care for an ageing population far exceeds the possibility of the unsustainability of other direct transfers (i.e pensions).

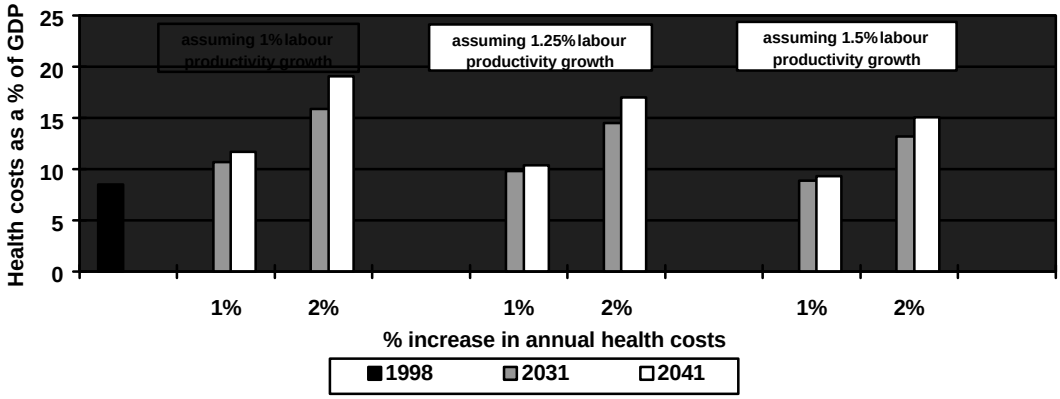
RIM projects (Rothman 1998) that, given a 1% annual growth in health costs above inflation, total spending on health care by governments will rise from the current position of about 8.5% of GDP to between 8.9% and 10.7% of GDP in 2031 and to between 9.3% and 11.7% of GDP in 2041.[4]

With a 2% increase in annual health costs , which RIM suggests as more indicative of prevailing trends, total spending on health is projected to rise to between 13.2% and 15.9% of GDP, or to about $117.8 billion in 2031. By 2041, a 2% growth in annual health costs would result in expenditure on health of between 15.1% and 19.1% of GDP, or, essentially, double existing health based expenditure (8.5% of GDP).

[4] variances are the result of assumptions about labour productivity growth.

It would appear then, that if the growth rate in the cost of health services can be limited to 1% per annum above inflation, or to a level not dissimilar to projected base case[5] increases in pension costs, then the sustainable provision of health services for any given age group may be assured over the long term. However, if the annual growth rate in the cost of health is closer to 2% over the next half century, and the rise in the total cost of health amounts to between 6.6% and 10.6% of GDP above the current level as projected by RIM, the increase in the burden of future health costs would far exceed increases in pension costs. Such a scenario, which is not implausible if neither technological advancement or government initiative can reverse recent health cost trends, would definitely raise issues of sustainability.

Fig 7 - Projection of Total Health Costs as a Proportion of GDP

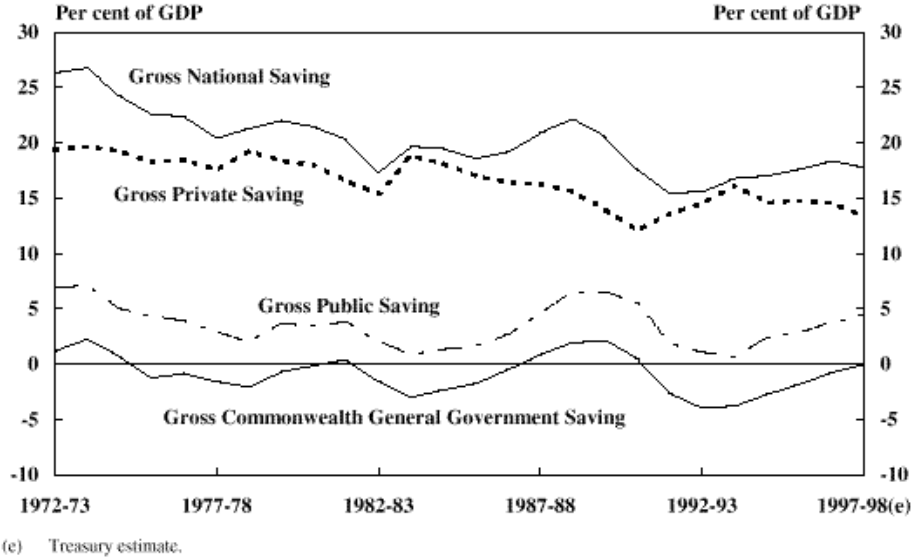


Data source: Rothman 1998

2.3 National Savings

Over the last three decades Australia's gross rate of national savings has declined progressively, falling to a low of just over 15% of GDP in 1991/92, and bumping along around that level since then. In his report on national savings, Dr Vince Fitzgerald (1993), identified that increasing the rate of savings in Australia was imperative if the level of investment required to ensure higher growth and more employment was to be reached without a further build up of foreign debt, and if the issues surrounding Australia's demographic transition were to be tackled adequately. The challenge, as defined by Fitzgerald remains, and if anything, has intensified.

Fig 8 -Gross National, Private and Public Saving



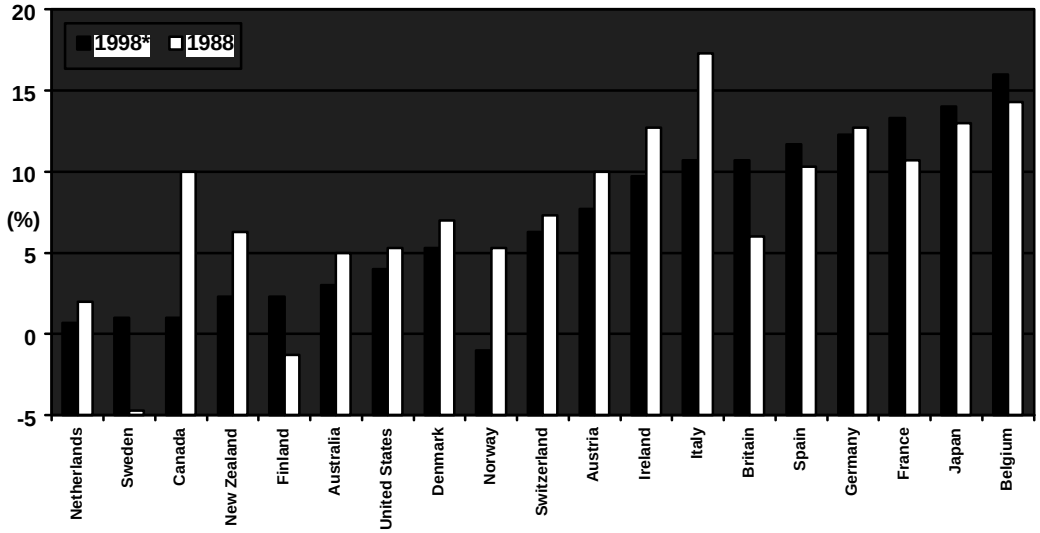
(e) Treasury estimate.

Source: Budget Strategy and Outlook 1998-99

[5] i.e RIM base case as described earlier

The 1998-99 Commonwealth Budget marks the recovery of public savings but private savings, particularly household savings, have sunk to a very low level. Australia is among the few OECD nations in the world to have experienced a decline in the level of household savings since 1988, with household savings forecast to fall to about 3% of household disposable income this year.

Fig 9 - Savings Ratios - Household Savings as a % of GDP



Source: OECD 1998 * Forecast

The need to boost national savings goes hand in hand with the indispensability of effective retirement income policy. However, effective retirement incomes policy requires any measures designed to positively impact on national savings to complement the existing three pillars (i.e. Government pensions, compulsory superannuation contributions, voluntary superannuation contributions) approach to retirement provision. To this end, tax advantaged savings instruments which are used to support long term savings should meet the criteria of:

- adding to both private and national savings;
- being preserved until retirement or for a lengthy period;
- not being able to be accessed for short-term consumption purposes; and
- not being an alternative to government funding of services best undertaken by government such as provision of a basic Age Pension or hospital services.

Unfortunately, against these criteria, neither political party has proposed effective policies to bolster either private or public savings beyond the compulsory superannuation system which has now been in place for some time.

How retirement benefits are funded and paid will have an important impact on both current and future levels of national savings.

2.4 Affordability of Tax Concessions for Superannuation

Given the element of uncertainty associated with the availability of public funds to meet the needs of future retirees, there has been a question mark placed of late on the ability of government to fund concessions to superannuation in the present.

There are different possible approaches to setting the benchmark for assessing whether the tax treatment of superannuation and other forms of saving is concessional and to what degree. One approach, favoured by the Treasury, treats all superannuation contributions as cash in the hand of the member, even though a member might not receive the benefit of the contributions for some decades, and even then may in some limited circumstances receive only part of the benefits of contributions.

An alternative approach which has strong theoretical and practical underpinnings is to apply a benchmark that tax should only be due when benefits are paid (that is, when the member may actually spend that money), and that taxes on contributions and fund earnings are inappropriate.

Using this latter approach analysis of official tax statistics indicates that in recent years superannuation has been overtaxed. On Access Economics'estimates:

- superannuation was concessionally taxed to the tune of a very modest $55 million in 1993-94 (compared to the Treasury prepared TES estimates of a large concession of $7,665 million in that year);
- superannuation was overtaxed by $803 million in 1994-95 (in comparison the Treasury TES estimates a concession of $5,770 million in that year); and
- superannuation was overtaxed by $775 million in 1995-96 (in comparison the TES estimates a concession of $8,315 million in that year).

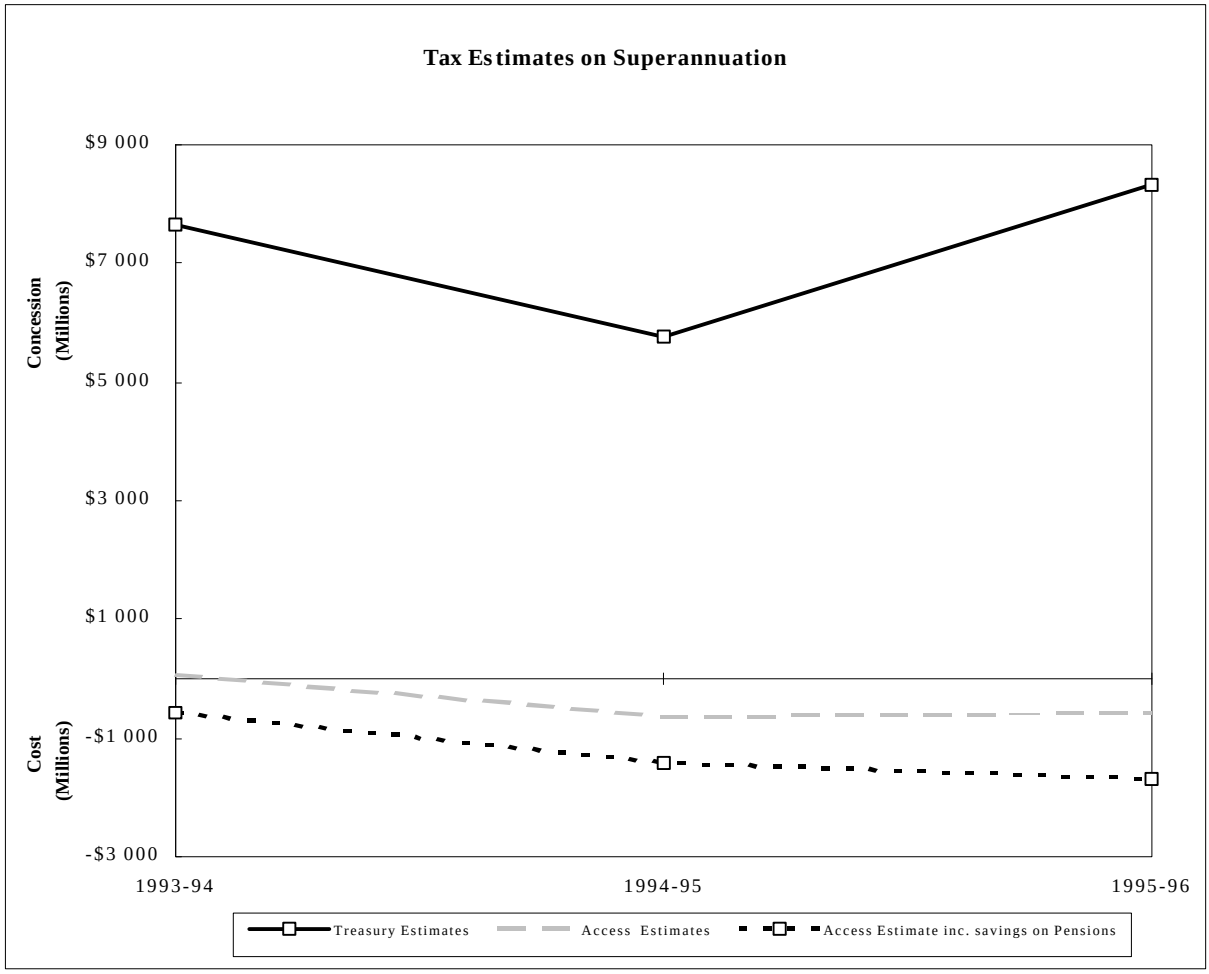
Given the large lift in superannuation tax revenue received by the government in 1996-97 (from $1,634 million in 1995-96 to $2,595 million in 1996-97), it is likely that the over-taxation of superannuation is growing.

2.4.1 Future Age Pension Savings

Apart from applying the right conceptual benchmark, the cost of any special taxation provisions relating to superannuation also can be offset in part by the savings on Age Pension and other social security expenditures that flow from increased self-provision through superannuation. On Access Economics'estimates, these savings are considerable. Self-provision through superannuation are estimated to have decreased government expenditures by $637 million in 1993-94, $623 million in 1994-95, and $924 million in 1995-96.

Taking into account these expenditure savings and applying the more appropriate expenditure tax basis for assessing tax concession, Access Economics estimates indicate that rather than being a drain on tax revenue, superannuation was overtaxed to the extent of $582 million in 1993-94, $1,426 million in 1994-95, and $1,699 million in 1995-96.

Figure 10 - The Cost of Superannuation Tax Concessions



Given the crucial role played by tax concessions in attracting voluntary savings for retirement and maintaining public acceptance for compulsory private retirement saving, it is important that accurate and meaningful estimates are calculated and disseminated. Superannuation has a key role in meeting the retirement income expectations of what is a demanding "babyboom" generation and in containing future Age Pension costs of government.

3. Retirement and Retirement Behaviour

"Retirement Behaviour is complex. Research has demonstrated that retirement planning and actual retirement decisions are influenced by many considerations (including health, financial, employment, lifestyle and psychological factors).[6]"

3.1 Retirement Behaviour

3.1.1 Retirement Age

Up until recently, the compulsory retirement and pension ages in Australia were 65 for men and 60 for women. In actuality though, retirement practises have reflected a far more complex set of behavioural patterns than can be encompassed by any mandatory aged based definition. The decision for any individual to withdraw permanently from the labour force will no doubt incorporate expected social parameters, but the ultimate decision will also hinge on a plethora of other considerations, many of which will be out of the direct control of potential retirees.

In R.M Cornish's "An investigation of the retirement behaviour of older Australians"(an ASFA commissioned study), survey[7] results indicate that over 85% of male retirees had in fact left the full time labour market before pension age, with retirement in the decade before they turned 65 the most common scenario for survey participants.

For women in the survey, withdrawal from the full time workforce before the age of 45 was the most typical retirement behaviour, with married women apparently far more likely to retire early than women who had never been married. For male participants on the other hand, no link between marital status and retirement age was observed.

Table 2 - Retirees by Age of Retirement

	Men (%)	Women (%)
Less then 45 years	10.9	49.0
45 years to 54 years	17.0	20.6
55 years to Pension age	57.8	9.7
Pension age	10.2	4.6
Beyond pension age	3.1*	5.1
Never had full time job	**	9.1
Don't know	**	1.9*
Total	100.0	100.0

Source: Cornish 1997 note: * corresponds to 10,000-40,000 cases
* corresponds to less than 10,000 cases

In an earlier and similar survey of retirement behaviour the ABS (1995) reported that 26% of men had retired at ages 65 and over, 32% between the ages of 60 and 64,

[6] Cornish 1997

[7] The survey was included in the ABS's Population Survey Monitor in February and May 1996. From the 6,265 fully responding households, a person was chosen at random. If that person was aged 45 to 74 years inclusive, details on retirement or retirement intentions were obtained. In total, 2,443 persons aged from 45 to 74 years provided information on their retirement or retirement intentions as at May 1996.

30% between 50 and 59 and 13% aged 49 and younger. In contrast, only 4% of women retired at an age older than 65, while 21% retired between 60 and 64, about 40% between 51 and 59 and the remaining third or so of retired women leaving the workforce before the age of 50 (Wollcot 1998).

3.1.2 Intended Retirement Age

According to the Cornish survey, the intended retirement age of those over 45 who had not yet left the full time labour force contrasted substantially to results indicating actual retirement age. Survey participants who were not yet retired were equally divided between those who intended to retire from full time work before pension age and those who intended to do so after pension age. As indicated above, the majority of respondents to the survey who were already retired left the full time labour market before pension age.

Patterns of retirement intentions were also typically associated with different levels of household income in the Cornish survey. Most commonly, the study notes, men who lived in low income households indicated that they intended to retire from full time work after they attained pension age while men who lived in high income households (defined as households where total annual gross income was $60,001 and over) mostly intended to retire before they reached pension age (Cornish 1997).

Of all those survey participants who intended to retire at a pre-pension age, many cited at least one lifestyle and financial reason as a contributing motivation (See table 4 overleaf).

However, as Cornish notes "It is interesting that more intending early retirees did not include financial reasons amongst the reasons they mentioned for their retirement intentions. In total, only 52 per cent of men and 28 per cent of women who were intending to retire before pension age implicated one or more financial reasons in their retirement intentions. This is surprising given that for the majority of these intending early retirees, retirement intentions were clearly predicated on the assumption that early retirement was affordable. In the case of men who intended to stop full time work before pension age, the vast majority expected to be self supporting, either through superannuation, other retirement income schemes, investments or part time work."

Table 3 - Reasons Cited for Retirement Intentions

	Intended Retirement Age			
	Pre-Pension Age		Post-Pension Age	
	Men (%)	Women (%)	Men (%)	Women (%)
Employment Reasons				
Will reach compulsory retirement age	5.8*	**	43.1	37.1
Able to get early retirement package	4.2*	**	-	**
Expect to lose job	**	**	**	-
Unable to get full time work	-	**	**	-
Those citing at least one	11.1	**	43.1	37.3
Financial Reasons				
Could get lump sum superannuation	17.8	11.1*	4.2*	6.4*
Could live on super till Age pension	4.7*	**	1.9*	**
Able to get government pension/benefit	**	-	7.8	12.4*
Can afford to retire	36.0	21.2*	10.2	19.7
Those citing at least one	52.5	27.7	21.7	37.9
Health Reasons				
Own health problems	6.8*	**	6.4*	**
Care for sick family member/friend	**	**	**	**
Those citing at least one	6.9*	**	6.5*	**
Lifestyle Reasons				
Stop while health still good	23.5	19.3*	10.5	6.9*
Retire with husband/wife	7.4*	17.8*	4.1*	6.4*
Spend more time with family/friends	16.5	15.7*	11.8	12.2*
Spend more time doing other things	36.5	36.2	16.6	22.3
Want part time work	8.0*	11.6*	2.1*	8.6*
Do not like job	**	**	-	**
Those citing at least one	57.6	81.9	30.3	38.9
Other	12.3	**	8.9	9.5*
Don't know	**	**	**	**
No reason	**	**	4.3*	**

Table 4 - Reasons Cited for Retirement

	Retirement Age			
	Pre-Pension Age		Post-Pension Age	
	Men	Women	Men	Women
	(% of Totals)		(% of Totals)	
Employment Reasons				
Reached compulsory retirement age	6.4	2.5*	68.3	36.1
Able to get early retirement package	12.8	**	**	**
Lost my job/business closed	8.5	19.3	**	11.8*
Unable to get full time work	7.7	3.2*	9.9*	**
Financial Reasons				
Could get super lump sum/pension	3.5*	2.1*	**	**
Could live on super till Age pension	2.4*	**	**	-
Could get Government pension/benefit	9.3	**	20.4*	10.7*
Could afford to retire	11.2	8.4	**	**
Health Reasons				
Own health problems	38.5	29.2	**	13.8*
Care for sick family member/friend	6.2	7.7	**	**
Lifestyle Reasons				
Stopped while health still good	2.4*	2.8*	10.2*	**
Retire with husband/wife	3.3*	8.4	**	16.5*
Spend more time with family/friends	**	8.2	**	**
Spend more time doing other things	4.2*	7.3	**	6.7*
Wanted part time work	2.0*	5.6*	-	**
Did not like job	2.5*	1.8*	-	**
Other	5.7	12.0	-	6.1*
Don't know	-	-	-	**
No reason	**	**	-	**

Source: Cornish 1997 *Note: Totals do not add to 100% due to multiple mentions.*
** corresponds to 10,000-40,000 cases ** corresponds to less than 10,000 cases.*

3.1.3 Reasons for Retirement

Despite the progressive abolition of compulsory retirement in all Australian states except Tasmania, a large proportion of retirees state that they have exited the workforce because they have "reached compulsory retirement age" (see table 4 previous page).

In the Cornish study, "reached compulsory retirement age" was the most likely determining factor influencing the retirement behaviour of both men and women who had retired post-pension age. 68.3% of male post-pension age retirees and 36.1% of female post-pension age retirees cited this as a reason behind their decision to retire. A small proportion of those who had retired pre-pension age also stated that reaching a compulsory retirement age affected their decision to leave the workforce.

Of those who left the workforce before pension age, Cornish notes that health reasons, as well as problems with employment and the availability of retirement packages, significantly influenced the decision to retire "early". However, the reasons behind women's experience of early retirement were not necessarily equivalent to men's. For example, Cornish notes "whilst access to an early retirement package was an important reason cited by the men who retired before pension age, few of their female counterparts reported this reason. This is not surprising given that men and women tend to lead their working lives in different ways, with men more likely to fit the categories typically offered early retirement packages".

Many retirees, and men in particular, also decide to retire early after a period of unsuccessful job seeking. The Cornish study reveals the period between 1992 and 1996 as specifically indicative of a deteriorating labour market for older workers.

Table 5 - Retirement Behaviour: Those Who Retired Before Pension Age By Estimated Year of Retirement (a)

Estimated Year of Retirement	Men (%)	Women (%)
1983 - 1988 % who looked for FT work before retiring	5.0*	-
1989 - 1991 % who looked for FT work before retiring	10.1*	**
1992- 1996 % who looked for FT work before retiring	23.1	8.6*

Source:1997

Note: * *corresponds to 10,000-40,000 cases*
** *corresponds to less than 10,000 cases.*
(a) Estimates of the number of years since retirement were derived by the ABS based on the information on the age at retirement and age at the time of the survey.

According to Cornish "The male discouraged job seekers who had retired early over the period from 1992 to 1996, typically retired after a sustained struggle to find full time work. On average, these men reported that they had stopped looking for full time work approximately 3 years after they had finished their last full time jobs.

The deterioration in the labour market for older male workers is also demonstrated by the increase in the rate of employment problems experience exhibited by male

early retirees. A staggering 50 per cent of all men who retired early over the period from 1992 to 1996 demonstrated evidence of employment problems. The effect of recent public and private sector restructuring and rationalisation is evident in the finding that 20 per cent of all men who retired before pension age over this period reported that an early retirement package was a reason for their retirement.

In total, approximately four in five men and two in three women who retired early over this period reported retirements consistent with the concept of induced early retirement. Such a high proportion of early retirements apparently initiated by factors beyond individual control has implications both for national retirement incomes policy and for labour market policy. This is aside from the devastating consequences for individuals who find themselves in a situation where retirement occurs as a result of reasons beyond their control and at a time not necessarily of their own making."

The Australian Bureau of Statistics also notes the effect of deteriorating employment prospects for older people on the decision to exit the labour force. A study of retrenchment and redundancy undertacken by the ABS in 1997 indicates that 7% of individuals aged 18-64 who had held a job in the three years to 30 June 1997 had been retrenched or made redundant on one or more occasions in that three year period. Of those in the 55-64 age group who had experienced retrenchment or redundancy in the three years to 30 June 1997, almost 24% were unemployed at July 1997 and 43.5%, or two and a half times the proportion in any other age group, had in fact left the labour force. The proportion was even greater for women in this age group, with 63.5% no longer in the labour force as at 1 July 1997.

The ABS study also found that of those persons still classified as unemployed as at 1 July 1997 after being retrenched or made redundant sometime in the previous three years, individuals in the 55-64 age group were likely to experience the longest period of unemployment. The average period of unemployment was 43 weeks for those aged 55-64 compared to 28 weeks for those aged 35-44 and 31 weeks for those aged 18-24.

3.1.4 Timing of Retirement

An examination of the reasons impacting on the retirement decision indicates two contrasting groups of early retirees. That is, those for whom the timing of the retirement decision was purely "voluntary," and those who although had a level of control over the date of their retirement, where nevertheless "induced" into leaving the workforce by factors external to their direct control.

Male pre-pension age voluntary retirees are most likely to retire because of their financial situation, while females in the same category are more likely to attribute their retirement decision to lifestyle considerations. Induced early retirees on the other hand, both male and female, most frequently cite health and employment related reasons as the major influence on the timing of their retirement decision.

Table 6 - All Reasons for Retirement Cited by Those Retiring Before Pension Age

	Voluntary Retirees		Induced Retirees	
	Men	Women	Men	Women
	(Per cent of All Early Retirees)			
Employment Reasons				
Reached compulsory ret. age	-	-	6.4	2.5*
Able to get early ret. package	-	-	12.8	**
Lost my job/business closed	-	-	8.5	19.3
Unable to get full time work	-	-	7.7	3.2*
Those citing at least one	-	-	33.9	25.1
Financial Reasons				
Could get super lump sum/pension	2.6*	**	**	**
Could live on super till Age Pension	**	**	**	-
Could get Govt pension/benefit	4.5*	**	4.7*	-
Could afford to retire	9.1	6.5*	2.1*	2.0*
Those citing at least one	15.1	8.8	7.1	2.0*
Health Reasons				
Own health problems	-	-	38.5	29.2
Care for sick family member/friend	-	-	6.2	7.7
Those citing at least one	-	-	43.9	35.8
Lifestyle Reasons				
Stopped while health still good	**	2.0*	**	**
Retire with husband/wife	2.9*	5.5*	**	3.0*
Spend more time with family/friends	**	4.8*	**	3.3*
Spend more time doing other things	3.1*	5.8*	**	**
Wanted part time work	**	4.9*	**	**
Did not like job	2.3*	**	**	**
Those citing at least one	8.3	21.5	3.6*	8.4
Other	4.0*	9.9	1.7*	2.1*

Source: Cornish 1997 *Note: * corresponds to 10,000-40,000 cases ** corresponds to less than 10,000 cases.*

The Cornish study also identifies that despite the nature of the factors influencing the timing of retirement, the ultimate decision to retire was more often than not an abrupt one. A result perhaps indicative of a society unaccustomed, or unwilling, to consider long term planning in an era of increasing and unexpected job insecurity.

Table 7 - When Was The Decision To Retire Made: Those Retiring Before Pension Age For Voluntary Reasons

	Men (%)	Women (%)
Less than 6 months before FT work stopped	32.4	46.6
6 months to less than 1 year before	17.7*	29.6
1 year to less than 2 years before	19.3*	9.3*
2 years or more before	18.4*	5.0*
Had no choice	**	**
Don't know	7.8*	6.8*
Total	100.0	100.0

Source: Cornish 1997

*Note: * corresponds to 10,000-40,000 cases*

*** corresponds to less than 10,000 cases.*

4. Income and Assets of Older Australians

"At 25 per cent of average male total earnings, the Age Pension bumps along just above what economic and social researchers regard as the poverty line in Australia"[8]

4.1 Retirement Income Policy

4.1.2 The Level of Benefits to be Delivered

An important benchmark for evaluating a retirement income system is the level of retirement income that is being sought and/or will actually be received. This can then be used to judge whether adequate superannuation and other savings are being under-taken. Accordingly, adequacy of retirement income cannot be divorced from the question of adequacy of contribution levels. Knowing where you want to get to is no use if the means of getting there are not considered

However, contribution rates are not the only important determinant of what will be achieved in terms of adequacy. Years of contributions, average salary received, age of retirement, and sources of other funds, fund earning rates and the rate of inflation will also impact on final retirement incomes. This makes the translation of an income replacement goal for retirement into an operational strategy difficult.

Costs of living for retirees need to be considered as well. Retirees are likely to have consumption patterns which differ from the population generally. This may have some implications for the indexing of retirement incomes. However, more importantly if a retiree faces relatively low or no charges for medical and hospital care, pharmaceuticals, nursing care, home and community care, housing and public transport then a reasonable lifestyle might be maintained on a relatively low income.

There also are differences in attitude between different age groups to what is an adequate retirement income. Older people, for instance, have their views conditioned by formative years in which adversity and low incomes were relatively common. For many who have already retired the level of the Age Pension and the level of financial assets and superannuation they have accumulated govern their retirement income expectations.

For younger people, outcomes are more subject to individual control given that savings and superannuation contributions can be influenced. Very few young people expect that they will rely upon a government pension in their old age, with the expectation of having their own significant income instead. For older people, the contrary expectation and realisation is the case.

4.1.2.1 - Is the Age Pension Adequate?

At 25 per cent of average male total earnings the Age Pension bumps along just above what economic and social researchers generally regard as the poverty line in Australia. For those in private rental accommodation the Age Pension, even with rental allowances, is not always enough to avoid what is usually perceived as

[8] ASFA, June 1998

poverty. The Age Pension is sufficient to sustain only a very modest lifestyle, with no major expenditures possible outside those funded by governments such as health or aged care.

Whether the current level of the Age Pension is enough is a matter that can be debated. It should be noted though that the current Governments decision to legislate the link to 25 per cent of average male total earnings was actually one of the largest items in the 1997 Budget in terms of future budgetary impact. With current constraints on the willingness or ability of governments to increase tax revenues it is unlikely that a significant increase in the Age Pension will be possible.

4.1.2.2 - Overseas Targets

What do other countries seek to achieve in terms of replacement in retirement of working age incomes, and what are the implications for Australia?

FitzGerald, 1994 and EPAC, 1993 indicate varying target replacement rates:

- Sweden - typically around 70 per cent with almost universal coverage;
- United Kingdom - between 20 to 25 per cent and 35 per cent, and significant numbers below the poverty line;
- Israel - flat rate of around 25 per cent of average wage and up to 70 per cent under occupational plans;
- Canada - between around 25 per cent of average earnings and 40 per cent or more for some who qualify;
- Japan - goal of around 50 per cent of gross earnings (bonuses included);
- France - 40 to 75 per cent;
- Germany - 40 to 45 per cent;
- Italy - 80 per cent;
- Netherlands - 60 per cent.

In most developed countries the minimum retirement income for an individual is around 20 to 25 per cent of AWE, and for a couple around 40 per cent. In some countries the minimum amount is at or below the poverty line. Target rates of income replacement can be as high as 70 per cent, but because only a proportion of retirees ever meet the conditions necessary to meet such targets, average retirement incomes for a single person in such countries seldom exceed 40 per cent of average weekly earnings.

In terms of goals for income replacement, while there are some examples of replacement ratios at or in excess of 70 per cent, such rates generally are not sustainable over the longer term when significant government funding is required. This remains the case even when specially designated taxes to finance benefits are in place. Target replacement ratios in excess of 40 per cent are more common.

4.1.2.3 - What do Australians Want and Deserve?

On the basis of what the current cohort of Australian retirees has done, a goal of 25 per cent of male average total earnings might be appropriate, as most retirees are on incomes at or only slightly in excess of that level. The main exceptions are the less than 10 per cent of retirees who are on pensions from relatively generous public sector or employer defined benefit schemes, or those who have accrued significant savings during their lifetime.

However, there are strong indications that the low levels of income in retirement for the bulk of current retirees is a matter of necessity rather than choice. When asked, Australians who are currently entering the work force typically aspire to replacement ratios of around 60 per cent, preferably with the option of this being paid from age 60 or thereabouts (Shirlaw 1997, ARISA 1997).

This intention is reinforced by the rule of thumb adopted by many financial planners, which suggests that around 60 per cent of gross pre-retirement earnings is the appropriate goal for those putting together a savings plan for retirement.

4.1.2.4 - What Have Australian Governments Specified as Targets?

The current Government has not publicly specified its goal for replacement incomes in retirement. However, so far as contributions are concerned it has maintained the timetable for raising the SG contribution to a maximum of 9 per cent. Taxation concessions and incentives are in place for further voluntary contributions, but there is no plan for compulsory employee contributions. The co-contribution proposed by the former government for low and middle income earners also has been dropped. The Government also has proposed that individuals earning between $450 and $900 per month be allowed to opt out from having superannuation contributions made on their behalf.

Projections using the AMP model of retirement income (Doyle, 1997) suggest that SG contributions of 9 per cent, which is the main compulsory element of the current Governments policies, would result in a replacement rate of 28 per cent after 30 years and 43 per cent replacement rate after 40 years. For a person on about AWE, this implies a total replacement rate of both super and Age Pension after 30 years contributions of around 40 per cent.

Additional saving by individuals in the form of a 3 per cent personal contribution to a balanced superannuation fund would lift the gross replacement rate by 9 percentage points in gross terms, or around 4 or 5 percentage points when the impact on the Age Pension is taken into account.

If a SG contribution of 9 per cent and a personal contribution of 3 per cent is taken as the Government's preferred outcome, this is consistent with a replacement rate of around 45 per cent for 30 years'contributions and over 50 per cent for 40 years' contributions.

4.1.2.5 - What Should be the Goal?

Retirement income provisions should aim at achieving much more than poverty alleviation or the achievement of a minimum benchmark income for all individuals. The guaranteed minimum by government for a single retired person of a retirement income of 25 per cent of male total average weekly earnings provides a base level of income which just meets the objective of alleviating poverty.

In conjunction with this should be private retirement income arrangements which on the basis of reasonable assumptions about lifetime working patterns and other earnings will deliver a total retirement income in gross, pre-tax terms for a single

person in excess of 50 per cent of Average Weekly Earnings. A level of 70 per cent would be more in line with the hopes and expectations of many in the population, but this may be difficult for the bulk of the population to achieve.

In order to avoid leakages from this private savings side of the retirement incomes system and to promote a comprehensive three pillars approach to retirement income generation, a number of characteristics should be attached to retirement benefits which receive the benefit of concessional tax treatment or other assistance from government. These include:

- being in the form of an income stream rather than a lump sum (apart from a modest sum to meet immediate or urgent expenses);
- providing reasonable protection against the financial consequences of longevity through being available for a period not dissimilar to life expectancy;
- providing protection for dependants through appropriate reversionary benefits; and
- involve a drawing down of capital rather than being a form of estate planning.

4.2 Income and Assets of the Aged

1994 income distribution survey data reveals that the average income of a retired household was $12,254 in 1993/94 compared to $45,088 for a prime-age worker household.

Similarly, RIM estimates (Brown 1996) indicate that in 1992/93 retirees over the age of 60 received, in total, income amounting to $20,130 million, with 76% of men and 90% of women in this cohort having individual total incomes (including government pensions) in the range from $5400 to $15000.

Table 8 - Individual Total Incomes - All Persons Aged Over 60

Females 1992-93

Total Income	60-64	65-69	70-74	75-79	80-84	85-89	90-94	95+	All
	% of all in age group								
$0-$5,400	5.7	2.7	1.9	1.5	1.0	0.7	0.7	0.8	2.6
$5,401-$10,000	64.6	66.6	69.0	70.3	68.5	60.4	48.2	45.4	66.6
$10,001-$15,000	16.8	21.7	23.2	23.6	26.2	34.0	41.8	46.9	23.1
$15,001-$20,000	4.6	4.4	3.3	2.9	2.8	3.1	4.8	3.3	3.7
$20,001-$25,000	3.5	2.0	1.1	0.7	0.6	0.7	1.2	0.9	1.7
$25,001-$30,000	1.5	0.6	0.4	0.2	0.2	0.3	0.8	0.7	0.6
$30,001-$30,000	2.2	1.0	0.6	0.3	0.4	0.4	1.5	1.3	1.0
$50,001-$75,000	0.8	0.5	0.3	0.2	0.1	0.1	0.4	0.3	0.4
$75,000-$100,000	0.3	0.3	0.1	0.1	0.1	0.2	0.3	0.2	0.2
$100,000 +	0.2	0.3	0.1	0.2	0.1	0.1	0.3	0.2	0.2
All (numbers)	268,321	283,223	255,456	200,288	139,892	71,864	27,609	7480	1,254,132

Males 1992-93

Total Income	60-64	65-69	70-74	75-79	80-84	85-89	90-94	95+	All
	% of all in age group								
$0-$5,400	7.1	3.3	1.7	1.9	1.3	0.8	3.1	3.7	3.3
$5,401-$10,000	50.3	54.3	58.8	63.5	62.8	59,5	45.5	37.3	56.6
$10,001-$15,000	9.6	20.1	22.4	21.6	21.7	26.0	25.9	29.3	19.0
$15,001-$20,000	4.1	6.0	5.3	4.5	5.0	5.1	6.0	7.8	5.1
$20,001-$25,000	4.3	3.4	2.0	1.6	1.6	1.9	2.8	3.1	2.8
$25,001-$30,000	4.3	2.8	3.6	2.0	2.6	1.9	2.5	2.0	3.1
$30,001-$30,000	12.8	6.3	4.4	3.3	3.4	2.8	8.7	10.4	6.5
$50,001-$75,000	4.0	2.2	1.1	0.9	0.9	1.2	3.3	3.9	2.0
$75,000-$100,000	1.7	0.7	0.3	0.3	0.3	0.4	1.3	1.6	0.7
$100,000 +	1.7	1.0	0.4	0.2	0.3	0.3	0.9	1.0	0.8
All (numbers)	196,010	264,534	199,092	137,334	79,161	31,871	9,903	1,858	919,673

Source: Brown 1996

4.2.1 Sources of Income

Government sourced benefits are the major component of income for Australia's aged, with such transfers accounting for over 67% of the total income of retirees in 1993/94 according to Income Distribution Survey Data. The data reveals a significant variance in the level of reliance on government support between retired and working households.

Table 9 - Composition of Total Income of Retired and Working Households

1993/94	wage & salary	own business	rental income	invest income	age pension	other aged pension	other govt income	super income	other income
Retired	0.0%	0.0%	4.5%	15.6%	39.9%	11.8%	15.7%	12.9%	0.0%
Working	85.5%	9.0%	1.4%	1.6%	0.0%	0.0%	3.1%	0.3%	0.1%

source: Bacon 1998

According to RIM (see table below), 73% of all Australians over the age of 60 received a pension benefit with 49% of these receiving a "full rate" benefit. 54% of women and 44% of men in this age group received a government pension at full rate while a further 27% of women and 20% of men aged over 60 relied on a part pension as part of their retirement income. RIM notes that the "proportion of older Australians receiving full rate pensions rises with age possibly as people run down their retirement savings so that some part rate pensioners become full raters and some non-pensioners become part rate pensioners." (Brown 1996)

Table 10 - Persons Aged 60+, by Age and Pension Status

Females 1992-93

Age	Age Pension Status (no. of Persons)			Age Pension Status (% of all)			
	Non Pensioner	Part Pensioner	Full rate Pensioner	Non Pensioner	Part Pensioner	Full rate Pensioner	Persons (All)
60-64	116,357	91,499	157,309	31.9	25.1	43.1	365,165
65-69	77,696	103,079	172,134	22.0	29.2	48.8	352,908
70-74	41,863	84,347	166,714	14.3	28.8	56.9	292,925
75-79	31,628	58,527	139,345	13.8	25.5	60.7	229,500
80-84	12,878	38,936	99,281	8.5	25.8	65.7	151,095
85-89	6,807	20,723	50,149	8.8	26.7	64.6	77,679
90-94	3,460	8,178	17,832	11.7	27.8	60.5	29,470
95+	996	2,375	4,727	12.3	29.3	58.4	8,098
All	291,686	407,664	807,490	19.4	27.1	53.6	1,506,840

Males 1992-93

Age	Age Pension Status (no. of Persons)			Age Pension Status (% of all)			
	Non Pensioner	Part Pensioner	Full rate Pensioner	Non Pensioner	Part Pensioner	Full rate Pensioner	Persons (All)
60-64	249,476	19,020	93,777	68.9	5.3	25.9	362,272
65-69	95,047	85,330	144,863	29.2	26.2	44.5	325,240
70-74	52,519	64,014	122,716	22.0	26.8	51.3	239,249
75-79	31,362	37,656	93,292	19.3	23.2	57.5	162,310
80-84	12,781	21,441	53,940	14.5	24.3	61.2	88,162
85-89	5,615	87,764	21,492	15.7	24.4	59.9	35,871
90-94	2,162	2,322	5,139	22.5	24.1	53.4	9,623
95+	545	373	883	30.3	20.7	49.0	1,801
All	449,508	238,919	536,100	36.7	19.5	43.8	1,224,528

Source: Brown 1996

The level of dependence on the age pension also varies considerably depending on the income of retired households, with Income Distribution Survey data indicating disparity in the composition of the total income of retirees from different income cohorts.

Table 11- Composition of Total Income of Retired Households by Income Cohort

Incomes of Retired Households 1993/94	wage & salary	own business	rental income	invest income	age pension	other aged pension	other govt income	super income	other income
$0-$10,000	0.0%	0.0%	0.9%	5.4%	68.9%	6.5%	17.2%	1.3%	0.1%
$10,000-$20,000	0.0%	0.0%	2.7%	9.9%	42.8%	18.6%	18.8%	7.9%	0.0%
$20,000-$45,000	0.0%	0.0%	10.1%	27.8%	11.1%	8.5%	11.4%	32.1%	0.0%
$45,000-$90,000	0.0%	0.0%	13.9%	46.9%	0.0%	0.9%	4.5%	28.3%	0.0%
over $90,000	0.0%	0.0%	0.0%	81.3%	0.0%	0.0%	4.4%	14.3%	0.0%

source: Bacon 1998

4.2.2 Assets of the Aged

The RIM Unit estimates the total amount of capital invested by retired Australians to be somewhere between $330 billion and $360 billion, or $28% of the nation's wealth (as of the March quarter 1995) (Bacon 1998).

As of mid 1992-93 the total non-housing, non-superannuation assets of retirees amounted to approximately $119 billion (Brown 1996). Interest bearing deposits, worth about $75 billion, and superannuation pension entitlements, valued at $19.5 billion, were the two largest components of the non-housing, non-superannuation assets of retirees aged 60 and over.

Table 12 - Composition of Non-Housing, Non-Superannuation Assets of Retirees Aged 60 and Over, mid 1992-93

Assets	Percentage
Allocated pensions	1%
Annuities	4%
Superannuation pensions	16%
Interest bearing deposits	64%
Shares & capital gain assets	2%
Business	2%
Non-investment assets	11%

Data Source: Brown 1996

4.2.3 Incomes from Superannuation - Private Pensions in Australia

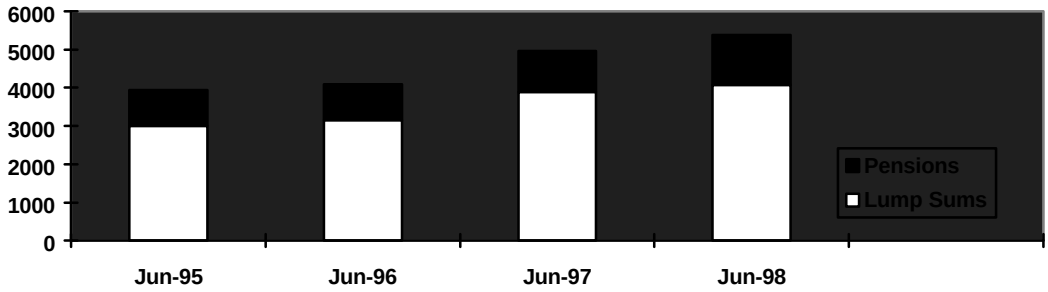
The distinguishing characteristic of the Australian superannuation system is the prevalence of lump sum payments rather than income streams on retirement. Lump sum benefits are generally paid by both defined benefit and accumulation funds, on retirement, death or permanent invalidity. The funds which still offer fund pensions as a benefit option tend to be a reducing number of public sector funds, and some older corporate funds. Where a lump sum option is also available, this is generally preferred by the beneficiaries.

Traditionally, lump sums were seen as a more tax effective, and more reliable benefit option. Since the early 1980s, increasing taxation of lump sums and other government measures has sought to redress the balance, but with only limited success. Some of the main reasons for continued attraction of lump sums are:

- flexibility in using lump sums for capital items or other purposes
- access to lump sums at early retirement (available from age 55)
- optimisation of eligibility for the age pension. This pension is publicly funded but subject to both income and assets means testing.
- certainty that the entire superannuation benefit is received by the contributor
- flexibility in estate planning
- a modest capital amount does not buy much of an income stream

Lump sums accounted for $4.1 billion or 75% of benefits paid in the superannuation industry (excluding transfers) in the march quarter 1998, with the remaining 25% or $1.3 billion being paid as pensions. The relative proportion of lump sum to pension payments has remained largely stable over time, indicating no apparent shift towards pension benefits paid directly from superannuation funds in recent years.

Fig 11 - Lump Sum and Pension Benefit Proportions



Data Source: ISC Bulletin March 1998

When Lump Sums are paid, their disbursement by retirees depends to a large extent on the age of the individual, with a significant proportion of those over the age of 45 using their lump sum to invest in an approved deposit fund, deferred annuity or other superannuation scheme.

Table 13 - Disbursement of Lump Sum Payment - Retirees Age 45+

	Age at retirement from full time work (years)			
	45-54	55-64	65+	Total
	-'000 -			
Received a lump sum payment	62.8	125.1	37.1	225.0
Rolled it over/invested in an approved deposit fund, deferred annuity or other superannuation scheme	20.3	48.9	9.6	78.8
Purchased an immediate annuity	0.0*	1.7*	0.3*	1.9*
Invested the money elsewhere/personal savings/bank	12.4	26.2	15.6	54.2
Paid off home/paid for home improvements/bought new home	6.1	21.6	4.6*	32.2
Bought or paid off car/vehicle	2.4*	4.1*	0.3*	6.8
Cleared other outstanding debts	3.1*	6.8	2.2	12.0
Paid for a holiday	0.9*	3.6*	2.5*	7.0
Assisted family members	0.2*	1.3*	0.0*	1.6*
Undecided	15.5	6.6	0.7*	22.8
Other	1.8*	4.4*	1.4*	7.6
Did not receive a lump sum payment	31.5	36.2	10.9	78.5
Did not know whether lump sum payment received	18.6	12.1	2.0*	32.7

Source ABS Nov 97

4.2.3.1 - Developing income streams market

Despite the general preference for lumps sums, there has been a growing interest in income streams as part of overall retirement income. This interest has been fanned by the development of new products which address some of the perceived disadvantages of lifetime pensions, as well as preferential treatment of traditional pensions in the superannuation tax regime and age pension means testing.

A major attraction of all superannuation income stream products is that currently, the assets held to support the income stream are tax exempt, as are earnings. This effectively allows recipients to defer the payment of the lump sum tax otherwise payable when the money is withdrawn. Superannuation income streams are subject to normal income tax when received, although there are some deductions and a rebate available under certain circumstances. Modifications to this tax treatment of assets supporting income streams was proposed by the Coalition in its election tax package.

According to the RIM (Tinnion 1998), 4% of all tax filers (about 395,950 people) and fewer than 11% of individuals over the age of 65 were in receipt of a superannuation or hon-government'pension in 1995-96. However, the over 65 age group accounts for approximately 62% of the total value of non-government pensions/annuities, with such individuals receiving, on average, a pension worth about $14,200 - slightly above the average for the population as a whole.

Table 14 - Superannuation Pensions and Annuities by Age and Taxable Income

Age	No. of individuals receiving Non-Govt Pension or Annuity	Total amount of Australian Non-Govt Pension or Annuities (millions)	Average Amount of Non-Govt Pension or Annuity received	Taxable Income	No. of individuals receiving Non-Govt Pension or Annuity	Total amount of Australian Non-Govt Pension or Annuities (millions)	Average Amount of Non-Govt Pension or Annuity received
Under 18	2,650	$19.1	$7,223.28	Negative	1,050	$9.3	$8,911.12
18-24	3,375	$7.7	$2,303.57	0-5,400	8,625	$46.8	$5,427.76
25-34	4,050	$30.5	$7,547.83	5,401-10,000	35,675	$206.6	$5,791.42
35-44	14400	$178.1	$12,370.41	10,001-15,000	94,325	$666.5	$7,066.72
45-54	31,875	$457.2	$14,344.21	15,001-20,000	69,425	$846.9	$12,200.19
55-59	39,850	$554.8	$13,923.58	20,001-25,000	52,575	$859.1	$16,341.90
60-64	61,875	$852.6	$13,779.63	25,001-30,000	36,600	$711.0	$19,427.85
65-74	156,700	$2,195.9	$14,013.80	30,001-50,000	64,850	$1,361.2	$20,990.61
75+	81,175	$1,165.6	$14,359.32	50,001-75,000	21,425	$455.8	$21,277.63
Total	395,950	$5,461.8	$13,794.40	75,001-100,000	6,475	$138.8	$21,444.42
				100,001+	4,925	$159.3	$32,353.69
				Total	395,950	$5,461.8	$13,794.40

Data Source: Tinnion 1998

4.2.3.2 - Income stream products

There are three main categories of income stream or pension like products, ie

- traditional fund pensions
- life office annuities
- allocated pensions and annuities

Each of these categories has its own characteristics and subject to its own tax and means test treatment. Estimates available on the importance of traditional pensions and annuities and allocated pension indicate that in 1992/3, less than 1% of retirement income came from allocated pensions, 2% from immediate annuities, and 8% from traditional superannuation pensions. By contrast, 66% of retirement income was provided by government pensions, and over 20% from non-superannuation investment income.

a) Traditional Fund Pensions

These pensions are generally restricted to the older defined benefit public sector and some corporate funds. In this situation, the pension is normally calculated on the basis a formula reflecting the recipient's service and salary history.

- Provided these pensions satisfy a set of standards imposed by the legislation regulating superannuation funds, they are classified as complying pensions. The standards include minimum pension duration, indexation levels and restrictions on commutation.

- Complying pensions give rise to higher superannuation benefit limits for recipients, twice those of lump sum benefits.

- Because it cannot be commuted, the capital value of complying life time pensions are not included in the asset test for age pension eligibility.

No statistics are available on the value of pension assets held by superannuation funds. However, in the June quarter 1998 pension payments by corporate, industry and public sector funds amounted to $969m, compared to retirement lump sum payments in the same quarter of $1909m. This apparently high proportion would largely reflect public service pensions remaining from earlier periods when lump sums were not available.

b) Traditional Annuities

These products, including life and term certain annuities, provide a guaranteed fixed or indexed income for life or the agreed term of the annuity. They involve the use or rollover of superannuation moneys to purchase an immediate annuity from a life office. Similar products are also available outside the superannuation environment.

If the annuity satisfies the Government's standards for complying pensions and annuities, it will attract the same advantages as the complying pension outlined above.

Funds under management in the traditional annuities market fell 2.4% from $3.8 billion in March 1998 to $3.7 billion by 30 June 1998 according to information provided by ARISA, the Australian Retirement Income Stream Association. This represented a growth during the previous 12 months of 8.8%. Gross sales in the last 12 months were $806m, only 16.6% of which was for life annuities, and the remainder for term certain annuities.

c) Allocated Pensions and Annuities

These income stream products were developed in response to perceived disadvantages of traditional pensions and annuities, such as the lack of access to capital, the lack of residual capital value after termination of the pension or annuity and the low implied earning rate for the assets supporting the pension or annuity.

Allocated pensions and annuities are effectively regular income payment plans from fully allocated superannuation or annuity accounts held by individuals. In order for the assets held in these special accounts to be tax exempt on any investment earnings, allocated pensions and annuities have to satisfy a special set of standards. These include:

- income payments to be made at least annually
- income payments to fall between a minimum and maximum amount based on the life expectancy of the recipient (to avoid estate building).

Allocated pensions and annuities differ from traditional ones in that

- there is continued access to the underlying capital in the account
- the account holder carries the longevity risk
- the accounts are generally investment linked, although some hybrid products with guaranteed returns are also available. A choice of investment strategies and /or managers is normally available.
- they do not attract the higher pension benefit limit, but do qualify for the pension rebate for benefits up to the lump sum limit.

Allocated pensions (also called cash back pensions) are generally provided as retail products by banks, fund managers and financial planners (master trusts). Allocated annuities are provided by life offices as retail products. Total allocated income stream assets (pensions and annuities) were about $14.8b by June 1998, of which allocated pensions represented $11.5b. The sector as a whole experienced a growth rate of 51% over the previous 12 months, with ARISA figures showing allocated annuities growing almost 30% faster than allocated pensions. Sales in the sector for the last 12 months, at just over $4.3b, were more than five times those of traditional superannuation annuities.

(d) Non-Superannuation Retirement Annuities

Funds under management for Life office annuities offered outside the superannuation system were $4.8b in June 1998, 16.9% up from the previous year. Sales over the previous 12 months were $1329m.

(e) Changes to the Definition of Income Streams

Legislative changes to the Social Security Act taking effect from 20 September 1998 will divide income streams into three basic categories:

- assets-test exempt income streams - those that ensure a steady drawdown over the whole retirement period and allow no further access to capital underlying the income stream. These will be exempt from the assets test.

- assets-tested income stream (long term) - those that allow access to capital but are still for a reasonably long term (more than five years). These will be assets tested, but will receive the same income test treatment as those in the first category.

- assets-tested income streams (short term) - those that allow access to capital and are for a short term only (five years or less). These will be assets tested, and will be deemed under the income test.

Table 15 - Australian Retirement Income Streams - Funds Under Management and Gross Sales (30 June 1998)

TYPE OF RETIREMENT INCOME STREAM	TOTAL $ BILLION	TOTAL MARKET SHARE %	CHANGE IN FUM OVER LAST 3 MONTHS %	CHANGE IN FUM OVER LAST 12 MONTHS %	SALES IN LAST 3 MONTHS $	CHANGE IN SALES OVER PREVIOUS 3 MONTH PERIOD %	SALES IN LAST 12 MONTHS $ MILLION	AVERAGE PURCHASE PRICE IN LAST 3 MONTHS $
ETP RETIREMENT INCOME STREAMS[9]								
➲ ALLOCATED INCOME STREAMS								
ALLOCATED PENSIONS	11.537	49.5	+16.3	+45.5	734.0	+25.5	2877.0	94,700
ALLOCATED ANNUITIES	3.244	13.9	+6.6	+74.1	324.0	+5.5	1423.0	107,400
TOTAL ALLOCATED INCOME STREAMS	14.781	63.4	+14.5	+51.0	1058.0	+18.6	4300.0	98,200
➲ ANNUITIES								
TERM CERTAIN (NO RCV)	Total for this category	Total for this category	Total for this category	Total for this category	14.0	-6.7	90.0	54,400
TERM CERTAIN (PLUS RCV)					77.0	-22.2	582.0	57,200
LIFETIME					19.0	+5.6	134.0	69,300
TOTAL ANNUITIES	3.700	15.9	-2.4	+8.8	110.0	-16.7	806.0	58,600
TOTAL ETP RETIREMENT INCOME STREAMS	18.481	79.3	+11.1	+40.1	1168.0	+14.1	5106.0	92,300
NON-ETP RETIREMENT INCOME STREAMS[10]								
➲ ANNUITIES								
TERM CERTAIN (NO RCV)	Total for this category	Total for this category	Total for this category	Total for this category	50.0	-30.6	333.0	42,100
TERM CERTAIN (PLUS RCV)					151.0	-21.3	957.0	91,500
LIFETIME					8.0	0.0	39.0	65,900
TOTAL NON-ETP RETIREMENT INCOME STREAMS	4.840	20.7	-1.0	+16.9	209.0	-23.2	1329.0	70,600
TOTAL RETIREMENT INCOME STREAMS	23.321	100.0	+8.0	+34.6	1377.0	+6.2	6435.0	98,200

Source: ARISA - Australian Retirement Income Streams Report[11]

[9] Retirement Income Streams purchased with an Eligible Termination payment (ie Superannuation moneys)
[10] Retirement Income Streams purchased with non-superannuation or ordinary moneys
[11] The ARISA Retirement Income Streams Report is the copyright of the Australian Retirement Income Streams Association ACN 059 367 289

4.2.3.3 Major players

Major players in the allocated pension/annuity and traditional annuities industry include most of the major life offices, banks and as well as specialist fund managers and master trust providers (particularly in the allocated product area). The market for income stream products is very competitive, with some 42 managers active in the sector, of whom only 4 had funds under management in this are in excess of $1b. as at September 1996 according to a market survey published by Rice Kachor Research.

As at March 1996, the ranking of the top ten providers was as follows:

Table 16 - Income Stream Providers

Manager	$m under management	% market share
AMP	1,526	11.9
Citicorp	1227	9.8
Commonwealth	1185	9.2
MLC	1003	7.8
National Mutual	$719	5.6
Norwich	666	5.2
Bankers Trust	632	4.9
AM Corporation	598	4.6
Colonial	551	4.3
ANZ	544	4.2
Market Total	12,839	100

4.2.3.4 - Cost structure

The range of fees and charges varies considerably between products. For allocated pensions/annuities, these might include some or all of the following:

- contribution charge (entry fee): from 0 to 5%, depending on size of deposit. Some may be rebated to investor.
- Administration fee: - eg $6.25 per month
- Income payment fees: eg $3 per payment
- Withdrawal fees: eg $60 per buy/sell, or 1% to 4% of withdrawal reducing over time.
- Switching fees: eg $20 per switch, or buy/sell spread.
- Investment Management fees: ranging from 0.6 to 2.5% of assets, depending on investment choice.
- Other, eg trustee costs from 0.2 to 0.35%.

4.2.3.5 - Prospects

At present, retirement income streams represent only some 5% of the overall superannuation assets. The ongoing demand for these types of products is very much dependent on the extent to which government policy and regulation promotes income streams through its tax and social security measures.

Within the sector, demand for particular types of income streams vary both with the requirements of government regulation, and the investment returns on different types

of products. Where allocated pensions grew particularly fast prior to July 1994, when there was a change in government rules, fixed rate term certain annuities have been a growth area in the last year or so. The future treatment of allocated pensions for age pension purposes will be particularly important.

The Colonial Group (Corbett 1998) has forecast that sales of income stream products will grow from $6.0 billion in 1998/99 to $8.0 billion in 2001/02. They also forecast income stream product funds under management to rise from $25.1 billion in 1998/99 to $43.6 billion in 2001/02.

Ultimately, the growth of income stream products is also dependent on the size of overall benefit with which people enter retirement. Currently, around $15 billion leaves the superannuation system as ETPs each year. As the system matures the total amount and average amount will increase. However, at present the income streams market tends to be of greatest interest to relatively high net worth individuals. The benefits accumulated by those receiving only compulsory contributions are unlikely to be worth converting to income streams for a decade or two.

5. Discussion

5.1 The Demography of Australia's Future Retirees

Australia is among the demographically younger of the highly developed nations of the world, but like most developed countries is confronted with the social and economic consequences associated with a large and rapidly growing aged population. By the middle of next century the number of aged Australians is expected to double reaching approximately 5.5 million, or more than 20% of the entire population. The highest annual rates of growth in the proportion of the aged population are expected to occur between 2011 and 2021 as the cycle of baby boomers moving through there retirement years reaches its peak. By this stage the policies implemented to meet the needs of an older population will either begin to bear fruit or will be exposed as inadequate. With the demography of Australia's future retirees evident for some time now, the policies required to ensure adequacy must at this point become the focus.

5.2 The Economics of Ageing

Meeting the needs of a projected demographic transition presents a number of uncertainties. These include:

- **that the funding of aged based services and pensions at the level desired by future retirees may place undue and burdensome pressure on any one cohort of current or future labour market participants**. The ratio of those aged over 65 to the number of people actually working is projected to rise to 0.42 by 2024-25 and 0.54 by 2059-60, representing a substantially increased fiscal responsibility on those of working age;

- **that government revenue may be insufficient to fund aged based services and pensions at the level desired by a burgeoning cohort of future retirees**. EPAC projections indicated that welfare expenditures would, in the absence of compulsory superannuation, rise from $23 billion in 1989 to $105 billion in 2051. Without compulsory superannuation and tax concessions for voluntary retirement savings, rates for income and other taxes would eventually have to rise by up to 20 per cent in order to provide even basic retirement incomes;

- **that the levels of saving and appropriate investment in Australia may not be adequate to provide a comfortable retirement for the large number of future retirees;**

- **that governments may relinquish there commitment to funding concessions to superannuation in the present;**

Australia's retirement system has done much to address these concerns in the last two decades. With a basic age pension legislated to move in line with community standards, compulsory superannuation coverage for almost all employees, and preferential tax treatment for retirement savings, Australia is seen as a role model by many other countries. However, these foundations are beginning to be compromised, and with them a comprehensive and coherent approach to age based policy setting. It is time to restate and recommit to the objective of a retirement income strategy.

5.3 Retirement and Retirement Income

Retirement Behaviour is complex. Research has demonstrated that retirement planning and actual retirement decisions are influenced by many considerations (including health, financial, employment, lifestyle and psychological factors)[12] and that the decision to retire is often an abrupt one, made without due planning and consideration. Studies have also indicated that over 85% of men withdraw from the full time workforce before pension age while almost 50% of women leave the full time labour market before the age of 45. Four in five of these men and two in three of these women will exit the labour market for reasons beyond there direct control, indicating significant consequences for retirement income policy. Any commitment to the objectives of a retirement income strategy must take these factors into account and ensure that adequate incentives are in place to produce an outcome with long term retirement income generation as the primary goal.

To this end, the ASFA Blueprint for a National Retirement Income Policy suggests that a number of characteristics should be attached to retirement benefits which receive the benefit of concessional tax treatment or other assistance from government. These include:

- **being in the form of an income stream rather than a lump sum** (apart from a modest sum to meet immediate or urgent expenses). As the main aim of retirement income policy is to provide sufficient income to maintain an adequate standard of living for retirees throughout their retirement, a benefit paid in the form of a regular income stream would appear to be the logical ideal solution. Lump sums, especially when paid early, only exacerbate the possibility of leakages from the retirement income system;

- **providing reasonable protection against the financial consequences of longevity** through being available for a period not dissimilar to life expectancy. The large number of people experiencing an induced retirement at a time prior to their choice or expectation indicates, that even without consideration of trends in mortality, retirement income will increasingly have to be paid for longer periods.

- **providing protection for dependants** through appropriate reversionary benefits; and

- **involve a drawing down of capital rather than being a form of estate planning**. Lump sums offer particular flexibility in estate planning, especially when they are paid early and allow recipients the opportunity to optimise their eligibility for the age pension.

Translation of these general goals into detailed provisions will necessarily be a substantial task for both regulators and the sector. However, there are indications that both social security and taxation provisions are being reviewed by the relevant authorities with a view to making income streams more attractive to retirees. Another important goal will be to ensure that various types of income streams are consistently treated by tax and social security provisions.

[12] Cornish 1997

The superannuation industry will also need to review its practices and products. The move from defined benefits to accumulation schemes has led to the sector concentrating on the collection and investment management of contributions through the accumulation stage. Less attention has been given to how retirement income products are provided and marketed to those who take a benefit from accumulation funds. However, this is beginning to change as more individuals build up substantial balances in accumulation funds and seek a seamless transition from accumulation to a retirement income stream.

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