The hard conversation..

Introduction

Good morning and welcome to Day 2 of the ASFA Annual Conference

This conference is bringing together the best minds and ideas on pensions and superannuation from across the world. Together we can interrogate the forces for change impacting the sector and the implications they have for our superannuation fund members.

The future is not what it used to be.

In the 1920s it was predicted we would never sell more than 2 million cars because no more than 2 million people would be willing to work as chauffeurs. Today we are discussing driverless cars as an inevitable development

Earlier this year for the first time ever the electricity grid in the UK ran coal free (only for 24 hours but hey it's a start) ….In 1975 there were 250,000 coal miners in the UK, they were an important social group and brought down a government. There are now less than 2,000 coal miners in the UK (there are however 275,000 accountants!!).

The pace of transformation is breathtaking. The half-life of a technology degree is about 18 months

The rise of AI and Machine Learning

Technology - even the seemingly bland examples such as paper - has been at the heart of almost all the previous upheavals in our society – the agriculture revolution which killed off the last vestiges of feudalism or the industrial revolution which from 1848 unleashed changes that echoed down with often tragic consequences through Europe and indeed globally for 150 years.

Whether technologies such as AI, and Machine Learning will have equally dramatic consequences seems unclear. Will they decimate traditional jobs as some predict or will they also create new professions?

And what are the implications for retirement funding …

Will re-education, lifelong learning and re-training save us from career obsolescence or is that as some suggest a story we tell ourselves so we can sleep at night? Will Australians have to increasingly postpone retirement or will there be a scarcity of jobs for older Australians?

And maybe we should think about moving the contribution rate to 12 precent now as a hedge against the clear risks to our lifetime earnings capacity

And finally might AI and ML be the part of the solution to deliver ubiquitous affordable retirement advice and the cliché disruption we paradoxically crave and fear?

The rise of the gig economy

Over the last 12 months I have spoken repeatedly about the rise of the gig economy and its implications for superannuation. There are currently at least 2.7 million people in Australia with

some form of independent work arrangement, out of around 12 million employed persons. The rise of the gig economy will see an increase in the prevalence of so called independent work arrangements – most of which will be independent contract arrangements.

The gig economy is set to become more pervasive. ASFA estimates there are already around 100,000 workers in Australia who use web-based platforms to obtain work on a regular basis. Although this only equates to around 0.8 per cent of the Australian workforce, growth in such worker numbers in recent years has been strong. In Australia, as is the case in many other advanced economies, some platforms are recording double-digit rates of growth in worker numbers per year.

So how will this changing nature of work, the gig economy and insecure employment in general impact the employer-employee relationship at the heart of our occupational pension systems – superannuation? What can we do in response to that? Expand the coverage of the compulsory system or somehow encourage greater voluntary contributions?

Private Markets for Capital and an increasingly global asset allocation

Last week's quarterly APRA statistics highlighted the unique asset allocation at the heart of the Australian superannuation system. As at the end of the September 2017 quarter, 50.1 per cent of the $1.6 trillion investments were invested in equities; with 22.7 per cent in Australian listed equities, 23.5 per cent in international listed equities and 3.9 per cent in unlisted equities. Fixed income and cash investments accounted for 32.9 per cent of investments; 21.4 per cent in fixed income and 11.5 per cent in cash. Property and infrastructure accounted for 13.4 per cent of investments and 3.6 per cent were invested in other assets, including hedge funds and commodities. Over 30 per cent of assets were invested overseas.

Just 15 years ago the picture was much different. Only around 20 per cent of assets were invested overseas. Hedge funds, infrastructure and commodities were at very low levels. Even property amounted to only 5 per cent of assets.

How will our funds meeting the challenge of reducing concentration risk in the domestic market through internationalisation of their asset allocations and could the increasing role of private capital markets as a source of value creation and return end in tears?

Myth Busters

We will also a had a chance to slay some myths;

No - Superannuation isn't going to come up short as a public policy – by 2050 we will have reduced the reliance on the full or part aged pension to less than 50% - and only 2-3% of GDP fiscal burden in terms of government expenditure on the Age Pension.

Already 30% of those aged over 65 are completely self-funded. Around 23% of people aged over 65 have superannuation as their main source of income. Most importantly, superannuation is delivering retirement incomes far higher than the Age Pension.

No - Australians don't have more assets outside super than in super, and eating your furniture in retirement is not an option – even if the Grattan institute thinks it is.

For the great bulk of households (90 per cent or more) superannuation together with owner occupied housing are the dominant forms of saving to support living standards in retirement.

Downplaying the role of superannuation using flawed statistics and dodgy averages are debating tricks rather than sound public policy analysis.

No – Saving for retirement outside superannuation is not more efficient or effective – Super is still the best game in town for funding your retirement.

Concessional tax treatment of superannuation leads to more dollars of savings being invested and higher after tax investment returns from all forms of investment compared to being directly held by individuals.

And finally No – you wouldn't be better off having the Future fund manage default contributions – the stakeholders in the Future Fund can be proud of what they have achieved but the messiness and complexity of running a superannuation fund is not something they have a track record in and would reinvent the wheel.

While there is always room for improvement, the scope for substantial improvement is far less than some commentators claim. If there was some 'special sauce' that could be used to enhance investment returns, while at the same time reducing risk and fees, then every fund and investment manager would be keen to spread it thickly on their offerings. Being mostly in cash when the GFC struck is not a strategy that can be easily repeated.

The reality is that on a five year return basis and adjusting for taxation, $1 invested into the Future Fund in June 2012 would have returned $1.67 at June 2017. Comparatively, the average super fund would have returned $1.64. Scores of super funds have also performed more strongly than the average.

The industry has invested $900 million to implement SuperStream over the past five years. This has ultimately been funded by superannuants and Nationalisation would represent a waste of their retirement savings.

This 'scorched earth' mentality to policy development runs much deeper and pervades the current policy landscape. The Orwellian plethora of never ending inquiries, reviews, and regulation are in many cases at odds with a system that widely regarded as a global leader that has, by and large, served Australian's tremendously well.

In the long, slow wake from the financial crisis, we've lost the wood for the trees. The desperate scramble to regulate all and sundry is rendering collateral damage to system efficiency, productivity and innovation. Retirements will suffer if the industry continues to be slowly, but surely, constricted into submission.

We aren't going to shy away from the tough conversations either. We will address head on the need to redefine the category we operate in away from the Superannuation to ……Retirement Funding.

This might require some hard conversations, both in challenging the way many funds currently do things and also taking a critical look at proposals for change.

Trade Offs and Payoffs

Dan Ariely is helping us think about the big trade-offs in retirement funding. How do make sure our retirees and aging population in general is not under consuming to the detriment of their health and long term wellbeing.

How do balance the illiquid capital that is our family home(for those that will have them) with the needs of age care and independent living.

And how do we address the issue of over bequeathing and the conflicts which cognitive decline and wealth surface.

We should be carefully in assuming that we know better and that our fund members are foolish and misguided in wanting potential access to a significant amount of capital during retirement. Along with uncertainty about how long an individual will live is uncertainty about what financial resources they will need to deal with health and aged care. Insurance through superannuation currently largely ceases at age 65 as does the coverage of the National Disability Insurance Scheme. With better financial solutions in these areas might come more efficient drawdown of retirement balances.

Martin Lindstrom justifiably asked do we really understand our members. As we rush to embrace the "nudge" we need to be critical of what is a young 'science'. The rush to incorporate behavioural economic insights into products and public policy is admirable but we might need to do better in the long run by spending more time observing our fund members and the reality of their daily lives.

Retirement affordability lives in the aisles of our supermarkets, in the waiting rooms of our medical practitioners and in the lonely corners of our age care facilities. The industry may need to find its inner David Attenborough and embrace the more ethnographic and anthropological ahead of the dismal science. Super fund members are not just lab rats waiting to be tested on how they can best navigate a maze of products and tax legislation.

The right stuff

We also need to ask ourselves if our staff have the right stuff? If we aspire to be a world class retirement system we need to have the best talent and capability. Is our employment brand as a sector as compelling as we think? Are we drawing the best talent from across the world to our funds and are we prepared to find the best people to support our forays into overseas markets? What are we doing to develop and nurture the talent amongst our current employees? On the question of talent

…Hubris looms as our Achilles heel.

Rethinking the Category

Superannuation as a category restrains our thinking and our best endeavours. As a public policy construct it promotes undue focus on the legal, fiscal and tax issues. In member engagement it leaves us myopic to the very real needs of our members in retirement. But most importantly it has led (to borrow from David Brookes) to superannuation being over politicised and under moralised –

Yes we need to be held accountable, we need to have competition, we need transparency, we need strong governance but we also need to address the pressing questions which retirees think about in funding their retirement;

Will I have enough to live on?

Will I be able to look after myself?

Will I have to leave my home?

Where will I live?

How will I afford age care?

Who will look after me?…

These are the questions that many people want answered. The future isn't what it used to be…but you could make it better..!