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Supplementary Submission to Senate Standing Economics Committee Inquiry into the Superannuation (Objective) Bill 2016

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Summary

It's an uncomfortable truth for many that superannuation is not the sole source of retirement savings. In our original submission to the Senate Standing Committee on Economics Inquiry into the *Superannuation (Objective) Bill 2016* we showed that many households have large non-super assets (not counting the family home). We demonstrated that many households are not saving only through superannuation for their retirement incomes, and so it is inappropriate to set a purpose for superannuation that it alone will provide an adequate, or 'comfortable' retirement income for all Australians.

Many in the superannuation industry found it hard to imagine that they might not be at the centre of the retirement universe. Industry Super Australia, in a briefing note provided to the Committee, accused us of 'misleading' analysis that committed 'statistical sins'. Industry Super Australia claims that these 'statistical sins' lead us to overstate the importance of non-super savings, while not capturing the full diversity of household savings behaviour. But it is not our analysis that is misleading, as this supplementary submission to the Committee shows.

While we can debate the precise importance of non-super assets, and for whom, there is no way to deny that non-super savings are material for a significant number of Australians, even when excluding the family home and household effects. For many, superannuation will indeed be their dominant non-home asset, and the main contributor to a retirement income higher than the Age Pension. But for many others, non-super savings will make an important contribution to their retirement incomes.

Yet arguments about compulsory super contributions, and about appropriate tax concessions for super, typically assume that income in retirement will come *only* from Age Pension and super. Modelling of retirement income adequacy routinely ignores the contribution that non-super savings will make to the retirement incomes of many Australians. Analysis of retirement incomes, presented by Industry Super to this Committee, is no exception.

Our analysis suggests that today's 9.5 per cent Superannuation Guarantee and the Age Pension – ignoring *any* voluntary superannuation contributions and *all* non-super savings – will provide most workers with retirement incomes well above commonly used benchmarks of retirement income adequacy. Once non-super savings are taken into account, many workers are likely to have a higher standard of living when they retire in 40 years' time than during their working life. Increasing the Super Guarantee to 12 per cent, as currently legislated, risks worsening living standards for most workers to boost already sufficient retirement incomes.

Retirement income policy is a difficult and emotive topic. Those whose businesses depend on the size of super balances have a lot at stake. Understanding how people really save for retirement matters. Given the differences in how households save, no policy will strike the optimal balance between working and retirement income for *every* household. The best that policymakers can hope for is a reasonable balance between the different situations of a diversity of households. To achieve this, any objective for superannuation must acknowledge the diversity of savings behaviour, and the substantial savings outside of super that exist to support the retirement of many Australian households.

1 Grattan didn't sin

In our original submission to the Senate Standing Committee on Economics Inquiry into the *Superannuation (Objective) Bill 2016* we showed that many households have large non-super assets (not counting the family home).[1] This analysis demonstrated that superannuation alone shouldn't be expected to provide an adequate, or 'comfortable', retirement income for all Australians.

Industry Super Australia, in a briefing note tabled during the Committee's hearing, accused us of 'misleading' analysis that committed 'statistical sins'. Despite explicitly casting doubt on the competence of our analysis, this briefing note was supplied to the Committee without notice to Grattan Institute. It failed to reference a detailed rebuttal we had made to similar claims,[2] and on a number of occasions failed to reference our previous discussion of the precise issues that it raised.

This supplementary submission to the Committee addresses each of the claims made in the Industry Super Australia briefing note.

1.1 Averaging across households

First, we were accused of averaging across high-wealth and low-wealth households, and across young and old households, when highlighting the importance of non-super savings for retirement. Yet if Industry Super Australia had read our material more carefully they would have noticed we did the precise opposite of what they claimed.

Our analysis reported the distribution of non-super wealth for households of different ages and different wealth levels. Figure 2 of our original submission analysed the composition of household net wealth by household wealth decile *and* household age.[3] Figure 3 of the submission presented the share of non-home assets held in superannuation across the *full distribution of households* within each age group. This detailed analysis underpins our headline finding that many households of any particular age and level of income or wealth hold as much, if not more wealth outside super than inside super (not counting their home).

1.2 The family home

Second, we were accused of including the asset value of family homes in our analysis. But our analysis carefully distinguishes between owner-occupied and investment property, and highlights the importance of non-super wealth *excluding* the family home. In any case, to understand overall resources in retirement, the value of homes matters a lot. Many renting retirees are under financial stress; most home-owning retirees are not.[4] It is true, as Industry Super points out, that many retirees are reluctant to sell their home to fund their retirement. But there is no reason why housing assets shouldn't support living standards in retirement, as we[5] and many others[6] have argued.

[1] Daley and Coates (2017)
[2] Daley and Coates (2016)
[3] Previous work has presented similar breakdowns of non-super savings by household income *and* age. For example see Daley, *et al.* (2016).
[4] Daley, *et al.* (2016), p.5
[5] Daley (2015)
[6] Mather (2015)

1.3 Household contents and personal effects

Third, we were accused of including vehicles and household contents assets in our analysis. Yet all these assets support living standards in retirement, either as a potential source of income, or by providing in-kind services to their owners. That's why they are counted in the Age Pension assets test. And even when these components of household wealth are excluded – and we separated them out in Figure 2 of our original submission – many households of most age groups and levels of wealth report significant non-super income-producing assets.

1.4 Household-level analysis

Fourth, we were accused of including the assets of children and any other adults living in a household outside the members of any couple. It's true that analysing household assets includes the assets of some people that may be outside any couple in the household.[7] It's also true that it would be a mistake to assume that the assets of these third persons would be available to the members of the couple in retirement. But we have committed no such error. Our analysis focuses on the *relative* size of holdings of super and non-super assets, not the sum total value of all those assets. If the assets of these third parties weren't included in the household they would simply be classed in the analysis as an additional asset-holding unit in their own right. Neither their super nor non-super assets would disappear from the overall picture we present. And in any case, relatively few Australians live with an adult who is not their partner.[8]

And there are other good reasons to focus on assets at the level of households rather than individuals. Many Australians are living with a spouse or partner, where the household expects to pool their resources to fund their retirement together. This is why means tests in the social security system look at the combined income and assets of any couple, not just those of the individual, to determine eligibility for income support payments.[9]

Family law today also means that members of households who separate or divorce can expect an equal distribution of assets, including super: if one person takes the super in an equal distribution of the value of household assets, and the other takes the family home or other non-super assets, then they both have assets that can be used to support living standards in retirement. Where couples separated before family law was amended to account for super in divorce settlements, our analysis will already treat them as separate households.

1.5 Data sources for household savings

Fifth, we were accused of using a data source that under-reports superannuation assets. It is true that total superannuation account assets reported in the ABS Survey of Income and Housing 2013-14 ($1.4 trillion)[10] are lower than APRA data on aggregate superannuation funds under management for that period. But underreporting of assets in surveys is a common problem across

[7] The ABS defines a household as 'a person living alone or a group of related or unrelated people who usually live in the same private dwelling' (ABS (2016)).

[8] Only 2 per cent of Australian adults live in a household with adult family members other than a spouse, and a further 4 per cent of people live in 'group' households with unrelated persons. Grattan analysis of ABS (2015a).

[9] DSS (2017)

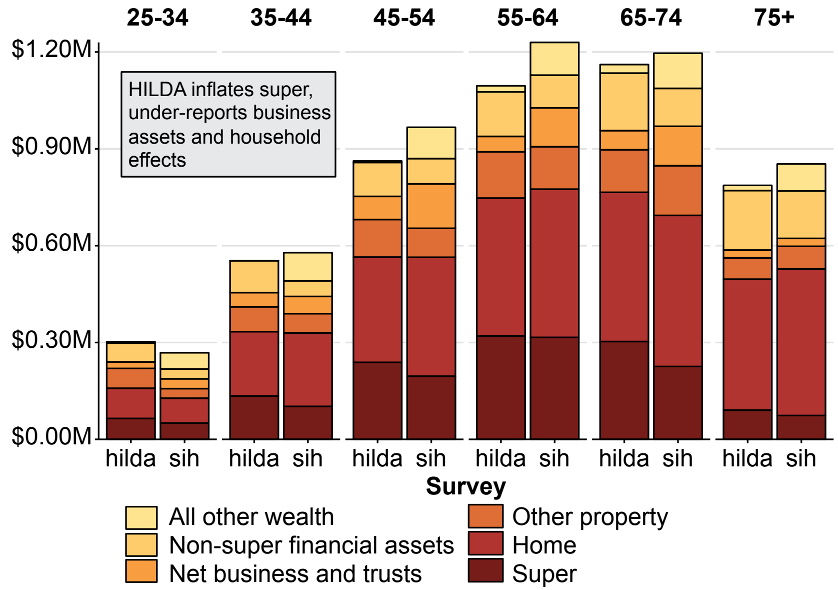
[10] Grattan analysis of ABS (2015b)

all asset classes, not just superannuation.[11] The problem is just more visible for superannuation, because a reliable aggregate exists, whereas it does not for other assets. There is no reason to assume that the level of underreporting is any less than for superannuation assets.

Comparing super and non-super assets as reported in the ABS Survey of Income and Housing with assets reported in the Household, Income and Labour Dynamics Survey (HILDA), we find that non-super savings are significant in both surveys (Figure 1). Importantly, superannuation assets in HILDA are benchmarked to reflect total superannuation assets as reported by APRA. Given that no benchmarking is possible for other asset data collected in HILDA, this likely has the effect of overstating the size of super relative to other household assets. We previously discussed these issues with the data in a 2016 publication.[12]

Figure 1: Both ABS and HILDA data show that households have large non-super savings

Household net wealth by age and source



Note: Home is net of related mortgage liabilities; other property is net of other property loans; business assets and trusts are net of related liabilities; all other wealth is net of all other liabilities; superannuation assets excludes some defined benefit schemes.

Source: Grattan analysis of ABS (2015b); HILDA (2015).

[11] For example, see Meyer, *et al.* (2015) on the issues of under-reporting of income in household surveys.

[12] Daley, *et al.* (2016).

1.6 Employees and the self-employed

Finally, Industry Super claimed that we didn't analyse employees separately from the self-employed. This is true, and it's also true that the self-employed tend to have more non-super assets – often including their own business. Industry Super has a point that the Super Guarantee is only relevant to employees, since the self-employed are not compelled to make super contributions. So it is reasonable to look at whether employees are saving enough to make up for any shortfall in super savings. But proponents of higher super savings often highlight the lower super savings of the self-employed while ignoring their non-super savings in order to claim that they don't have enough savings for retirement.[13] When considering the relevance of non-super assets to retirement in general, it is important to look at the self-employed as well.

[13] For example, see ASFA (2016).

2 Non-super savings are important on any cut of the data

In its critique, Industry Super presents analysis suggesting that superannuation is a more important part of retirement savings than we claim. Yet even this analysis demonstrates that non-super assets are an important part of the retirement incomes story for many Australians.

The main evidence from Industry Super analyses super's share of non-home wealth by decile of non-home wealth for employees aged 55 to 64.[14] It finds that only those people whose non-home wealth is in the top 10 per cent have more non-home wealth outside than inside super. But it all depends on how you see things. For half of Australians, average non-home wealth assets other than super are at least 25 per cent of their non-home wealth. That's a material fact when we're analysing retirement savings in total, yet it is one that proponents of higher super savings routinely ignore.

Even this Industry Super analysis is selective. It only looks at 55 to 64 year olds – the one age group who have *more* of their non-home assets in super than other age groups. Since the compulsory Super Guarantee was lower than it is today for most of this age group's working life, older households would have made lower compulsory contributions than younger age groups do now. But this 55-64 age group are more likely to have transferred non-super wealth into superannuation through voluntary contributions, because at their age they are not locking up their money for long.[15]

Industry Super's analysis also underplays how households pool the assets of their members. Many Australians are living with a spouse or partner, where the household expects to pool their resources to fund their retirement together. Yet Industry Super attributes assets only to individuals, not households. Since many assets are held in the name of only one person, this approach understates the assets that one member of a couple can access to fund their retirement.

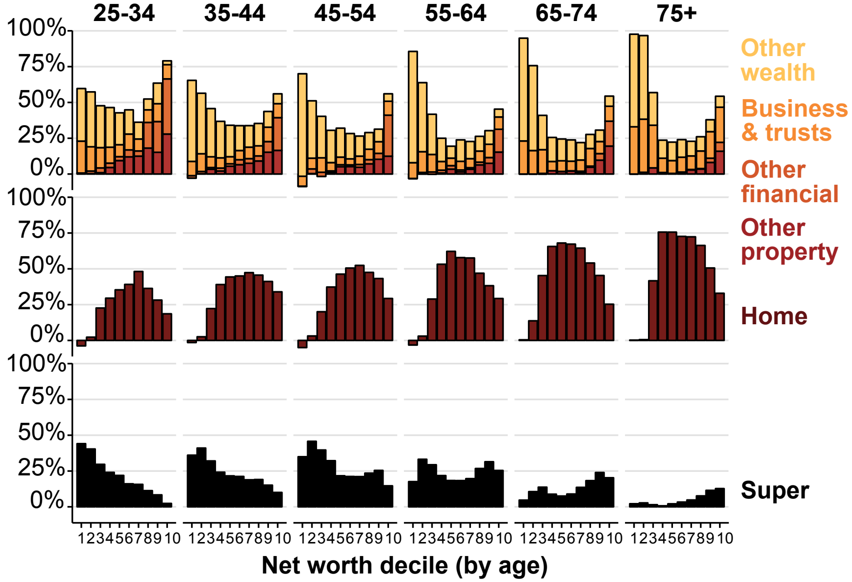
2.1 Non-super assets are important, even excluding the family home and household effects

To understand the significance of non-super wealth, it is more useful to look at all households, especially younger ones; to analyse households rather than individuals, because household analysis provides a more accurate picture of the resources available when one partner doesn't work much; and to consider all non-home wealth.

The analysis presented over the page – reproduced from our original submission to the Committee – shows that households of different ages *and* wealth levels hold substantial savings outside of superannuation (Figure 2). They might be in investment property, businesses and trusts, other financial assets such as shares and term deposits, or other household wealth such as vehicles and personal effects. Even excluding other household wealth, households of a given age and wealth level consistently hold between 10 and 20 per cent of their net worth in other financial assets.

[14] See Industry Super Australia (2017), Chart 1.
[15] Daley and Coates (2015)

Figure 2: Most Australians save as much outside superannuation as they do inside, across most ages and levels of wealth
Household net wealth by wealth percentile, age and source, per cent



Note: Home is net of related mortgage liabilities; other property is net of other property loans; business assets and trusts are net of related liabilities; all other wealth is net of all other liabilities; superannuation assets excludes some defined benefit schemes.
Source: Grattan analysis of ABS (2015b).

It is also true that for the least wealthy 20 per cent of households in each age group, super is invariably most of their non-home wealth. But in absolute terms, these super balances are small. At retirement, the Age Pension will inevitably dwarf them. Typically, these low-income households depend primarily on a full Age Pension for their retirement.

2.2 How *many* households have non-super wealth?

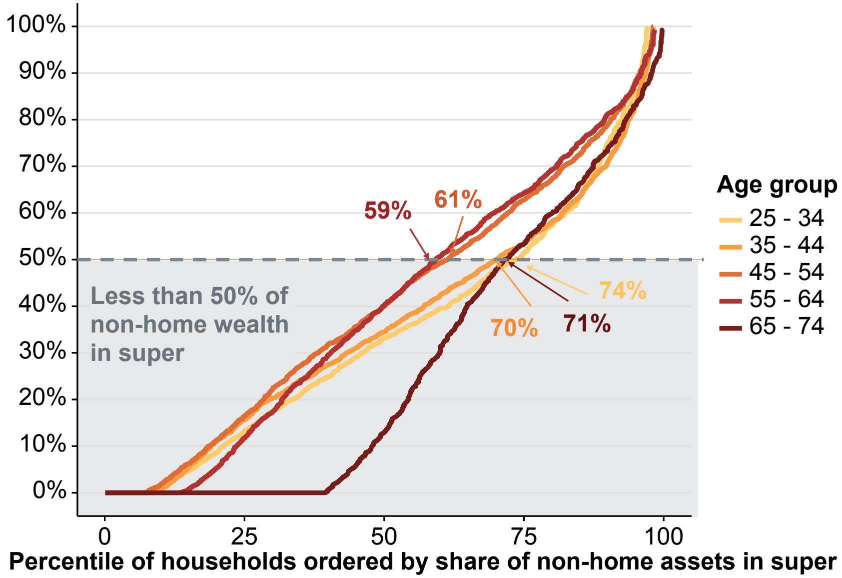
Another way to cut the data is to look not at the *average* wealth of particular age and income cohorts, but to ask what *proportion* of particular cohorts have particular levels of non-super wealth.

In doing this analysis, it's important to focus on households rather than individuals so that secondary income earners with few assets apart from any super don't obscure the real situation. The analysis presented below shows that more than half of households in each age group hold more than 50 per cent of their non-home wealth outside of super (Figure 3).

As Industry Super pointed out, there are differences between the self-employed and employees. An analysis of 45-54-year-old households where at least one income earner is an employee shows that 57 per cent hold at least half their non-home wealth outside of super (Figure 4). Since we are trying to understand retirement assets, it's relevant that almost four-fifths of these households hold at least 20 per cent – a material portion – of their non-home wealth outside of super.

Figure 3: Most households of each age hold less than half their non-home wealth in super

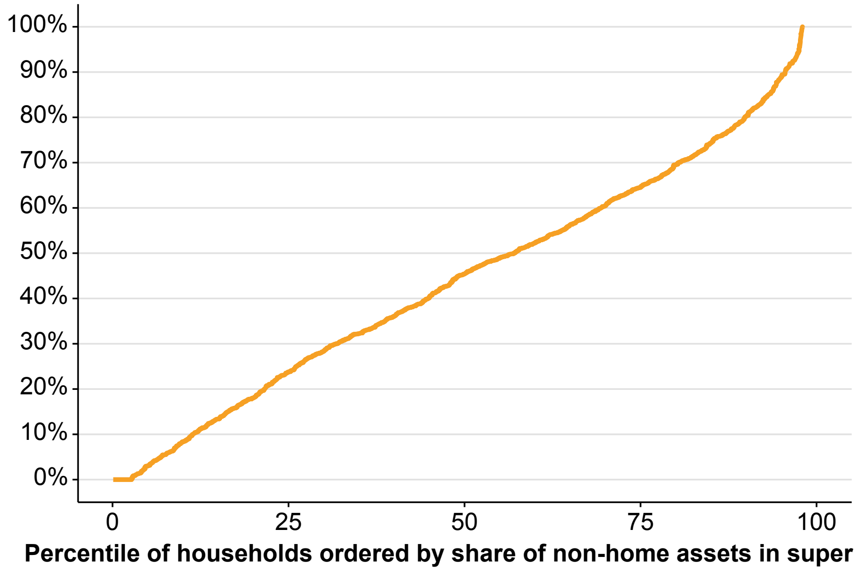
Super share of total non-home wealth by age of head of household, per cent of non-home net wealth



Notes: Non-home wealth excludes owner occupied housing and related mortgage liabilities, but includes investment property equity (net of related mortgages); superannuation assets excludes some defined benefit schemes; excludes households with no or negative non-home wealth.
Source: Grattan analysis of ABS (2015b).

Figure 4: Over 50 per cent of all 45 to 54-year-olds hold less than half their non-home wealth in superannuation

Super share of total non-home wealth, 45 to 54-year-old employed households



Notes: Non-home wealth excludes owner occupied housing and related mortgage liabilities, but includes investment property equity (net of related mortgages); superannuation assets excludes some defined benefit schemes; excludes households with no or negative non-home wealth; only includes households where at least one adult reports their main of income as employee income.
Source: Grattan analysis of ABS (2015b).

3 Non-super savings matter for superannuation and retirement incomes policy

While we can debate the precise importance of non-super assets, and for whom, there is no way to deny that non-super savings are material for a significant number of Australians, even when excluding the family home and household effects. For many, superannuation will indeed be their dominant non-home asset, and the main contributor to a retirement income bigger than the Age Pension. But for many others, non-super savings will make an important contribution to their retirement incomes.

3.1 Assessments of retirement income adequacy routinely ignore non-super savings

Yet arguments about compulsory super contributions, and about appropriate tax concessions for super, typically assume that income in retirement will come *only* from Age Pension and super. Modelling of retirement income adequacy routinely ignores the contribution that non-super savings will make to retirement incomes. For example, research recently undertaken by Industry Super Australia for the Committee for Sustainable Retirement Incomes, and re-published in their briefing note to the Committee, made precisely this assumption.[16]

This is simply not true for many people, as our analysis shows. And high-income and wealth households – those likely to run into limits on super tax concessions – are even more likely than other households to have large non-super wealth holdings.

[16] Committee for Sustainable Retirement Incomes (2016), p.6; Industry Super Australia (2017), pp.4-5.

3.2 Retirement incomes appear adequate with a 9.5 per cent Super Guarantee, even ignoring non-super assets

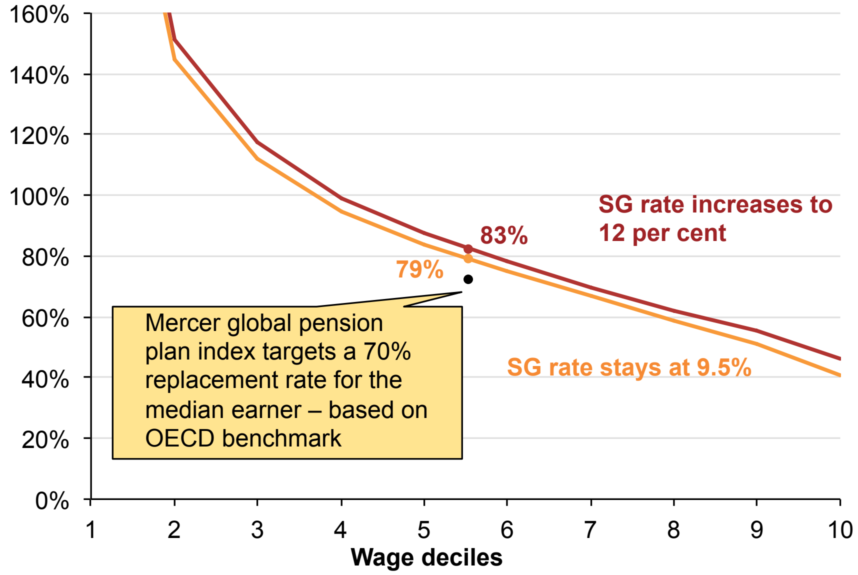
In fact, current levels of compulsory super contributions and Age Pension are likely to provide a reasonable retirement for most Australians.

If we project forward the retirement income for a median-income earner working for 40 years, and account for compulsory super contributions only – in other words, we ignore any voluntary superannuation contributions and savings outside of super – we find that today's 9.5 per cent Superannuation Guarantee and the Age Pension would provide the average worker with a retirement income equal to 79 per cent of their pre-retirement wage, also known as a replacement rate (Figure 5).[17]

About two-thirds of income earners can expect a retirement income of at least 70 per cent of their pre-retirement income – the replacement rate for the median earner used by the Mercer Global Pension Index and endorsed by the OECD.[18]

[17] These figures are broadly consistent with replacement rates published by the Treasury, which projected that a median earner aged 30 in 2014-15 would see a replacement rate of 80 per cent of their pre-retirement income, based on legislated increase in the Super Guarantee to 12 per cent (Morrison (2015)).
[18] Mercer (2015)

Figure 5: Under existing super policy, most will largely replace their pre-retirement income
Replacement rate of pre-retirement disposable income, per cent, based on a 30-year-old in 2016



Note: See original submission, Figure 4.
Source: Grattan analysis of ABS (2015b); HILDA (2015).

Once non-super savings are taken into account, many workers are likely to have a higher standard of living when they retire in 40 years' time than during their working life. This is before factoring in that many people have lower spending needs in retirement, particularly in the later stages of life when government covers much of their largest costs of health and aged care. Lifting the Super Guarantee to 12 per cent, as currently planned, risks compromising living standards for workers in order to boost retirement incomes that already appear sufficient.

3.3 The Superannuation Objective should recognise that super is not the only contributor to retirement incomes

Given the differences in how households save, no policy will strike the optimal balance between working and retirement income for *every* household. The best that policymakers can hope for is a reasonable balance between the different situations of a diversity of households. To achieve this, the policy debate must acknowledge the substantial non-super savings of many Australian households that will support their living standards in retirement.

There's no free lunch when it comes to superannuation. Boosting retirement incomes always comes at a cost: either workers have lower living standards while working; or governments give up more revenue for super tax breaks; or taxpayers pay more for pensions.

In setting an objective for superannuation, we must recognise that superannuation is only one part of our retirement incomes system.

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