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Policies for drawing down retirement saving in New Zealand: implications for the ageing of the population

AGEING POPULATION CONFERENCE 2005 - SIXTY-FIVE AND NOT OUT!

7-9 September 2005,
St Anne's College Oxford, UK

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"Converting assets to income in an orderly fashion will become an increasingly important issue for the ageing populations and economies of many nations."

(Wadsworth, Findlater, & Boardman, 2001, p.3)

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The New Zealand's two-pillar model

Universal basic pension

State

+

Voluntary saving

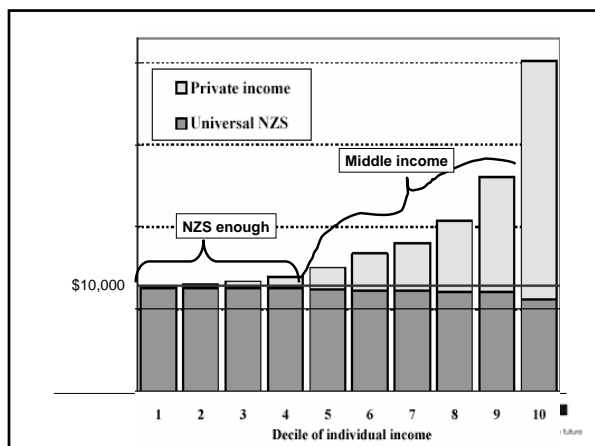
Private

Two legs are better than three?

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Public provision- basic pension

- Non-contributory, residency based
- Individually based
- Linked to wages
- Prevents poverty
- PAYG with some prefunding
- Tax funded
- Low administration

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Voluntary private provision

- No tax incentives (i.e. no bribes) !
- The level playing field for saving

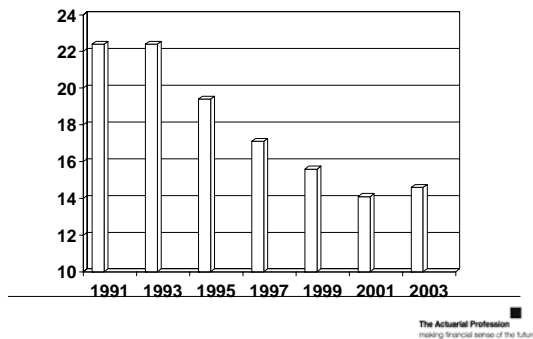
“The government is not considering upfront tax incentives. .. Their abolition in the mid-1980s represented sensible tax policy on both equity and efficiency grounds.”

(Minister of Finance, 2002a)

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Private pensions: a thing of the past

% Coverage in workplace schemes



The risks of middle-income retirement

Few mechanisms to protect extra savings against

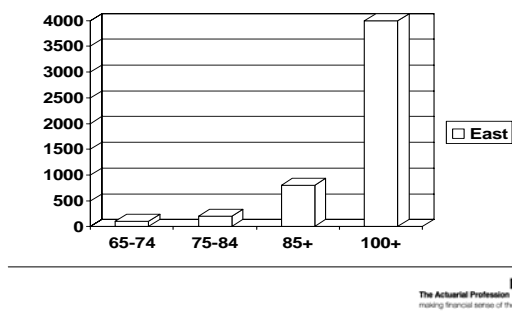
- Longevity
- Inflation
- Growth in living standards
- Too much capital tied up in housing
- Long-term care costs



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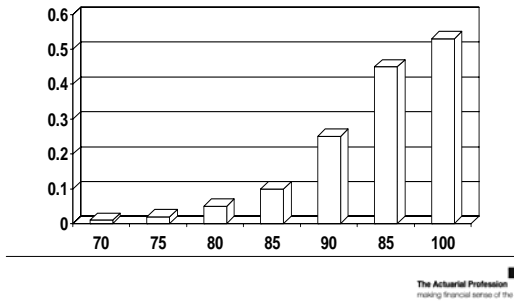
The coming crunch

Expected % growth of those over 65 by mid century

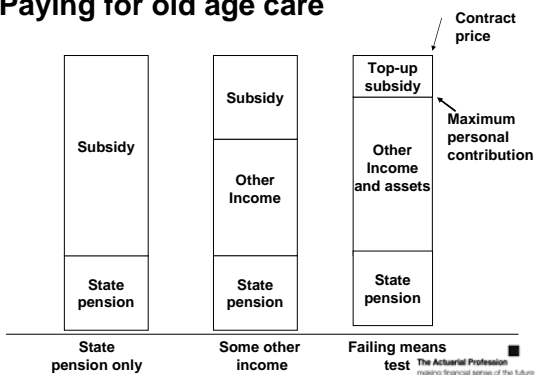


Uninsured risk for middle incomes

Probability of being in long-term care



Paying for old age care





The case for attending to drawdown phase

- Lump-sums are hard to manage
- Can be spent too early
- Assets can be gifted away
- Trusts encouraged
- Costs of older age can then fall on working age population

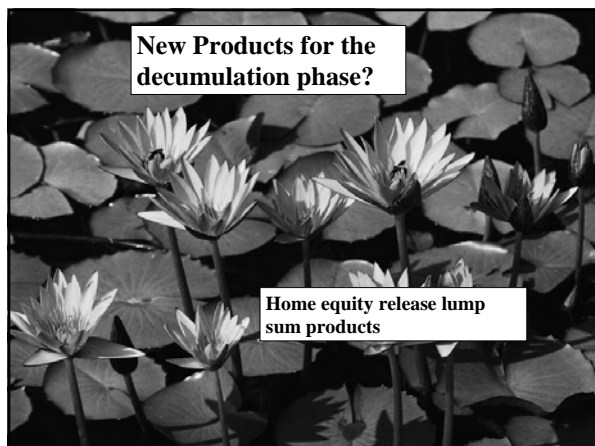
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Current annuities market almost non-existent

Life annuities

- **Appear expensive**
- **Poor value for women**
- **Timing is a lottery**
- **No protection from inflation**
- **No protection from growth in living standards**
- **Institutional risks and no guarantees.**

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What are they used for

Home improvements 47%
Car 33%
Extra income 32%
Holidays 29%
Gifts 24%
Repayments 24%
Goods 23%
Long term care 8%

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How risky are they?



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What are the risks not being addressed?

For the individual

- The need for regular ongoing income for the whole of life.
- The unforeseen need to move earlier than expected
- A compounding interest rate that can change

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For society-

- may be a way of avoiding the asset test for long-term care
- the government may become liable for a rest home subsidy in full.

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More intragenerational sharing required to

- Improve fairness
- Release extra resources

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What should be the government do?

- Identify the social advantages that might flow from annuities
- Explore integration of life annuities with long term care insurance
- Subsidise, support and regulate the market, or act as provider

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An ideal supplementary annuity would:

- Be good value for money;
- Be inflation-proofed;
- Be less of a lottery than is currently the case;
- Be gender neutral,
- Allow, in suitable cases, the use of part of the equity in owner-occupied housing for the annuity purchase;
- Include insurance for catastrophic care costs, especially long-term care costs

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A new product for New Zealand?

- Inflation-adjusted gender-neutral Life annuity of value of approx \$10,000 pa
- Increased on the determination of the need for long term care- say *annuity trebles*
- Paid for at age 65 with cash and if suitable, equity share in housing

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- Tentative costings suggest that this product is feasible
- Might look attractive to both men and women
- Cost of long-term care insurance modest

FOR NEW ZEALAND Subsidy to the decumulation phase may make more sense than subsidising the accumulation phase

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