

## Savings debate too narrowly focused

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There is an emerging consensus that increasing savings rates in New Zealand would improve productivity and prosperity by providing greater availability of capital for productive businesses. That recognition has led to calls for greater encouragement of saving, with compulsory savings among the policies being assessed by a Working Group. While savings policies can provide a valuable lift in capital available for productive investment, savings policies should also be connected with universal superannuation and with policies that promote productivity and wellbeing of older New Zealanders.

Australia has had much stronger savings policies than New Zealand, including compulsory savings, for a long time. Partly as a result, Australia had in 2007 gross savings at 23% of nominal GDP compared to 16% in New Zealand, it had average household net wealth of \$710K versus \$404K in New Zealand, and in 2008 had \$250K of productive capital employed per worker versus \$127K per worker in New Zealand.

Making saving compulsory is valuable, partly because people considering saving face a difficult decision. Savings may accumulate a lot over a working life but discount rates applied over 30 or 40 years mean that the future benefit is not highly valued by many younger people starting their working lives. The world in the future might not be as people expect and financial institutions may fail, so there is a risk that savings may not be available after several decades. As a result, many people choose to delay saving which results in low savings, poor accumulation of productive capital and high levels of debt. If enough people save too little then a heavy burden of supporting people in retirement will fall on future generations, or many retired people will be poor.

Savings policies should not be separated from retirement policies. Increasing compulsory saving obligations inevitably raises questions about retirement. If individuals will have more savings at the time of retirement, that alters the need for universal superannuation.

The equation for universal superannuation in New Zealand's future looks difficult. Today the life expectancy of a 65 year old is on average 85 years and life expectancy in New Zealand has been increasing by a few months per year over the last decade. In 2009 13% of New Zealand's population was aged 65 or older, supported by taxes from the 66% of the population aged 15 to 64. By 2031 21% of the population will be 65 or older and only 61% aged 15 to 64. Many people have pointed out that something must be done and options offered include lifting the retirement age or providing more flexible take-up ages, indexing payments to inflation rather than wages to slow the rate of increase, targeting superannuation payments or introducing some form of surcharge.

Historically, superannuation debates in New Zealand have become divisive, so making changes to universal superannuation is difficult, encouraging some governments to delay addressing the issue. Many older people legitimately feel they are entitled to

superannuation because they have paid taxes to contribute to superannuation for those who have gone before, and older people are an important voting constituency.

Despite that, we all have common interest in retirement policies that are affordable, sustainable, and ensure those who are retired have sufficient income. But we will not all benefit if the steadily aging population structure makes the current superannuation scheme unaffordable. If other countries perform better economically because they have high savings and investment levels we risk having our savers leave to join them, making the load even more burdensome for those who remain.

But extending the focus of debate to include fiscal and entitlement dimensions would still be too narrow. Our retirement savings model presumes that people work until age 65 and then stop working. It was set up when physical workers were exhausted at age 65 and stopping work was good for their health. Today, many people would prefer work options that allow them to progress from full-time to part-time work and then to retirement, possibly with retraining to update skills or to prepare them for a different kind of work.

Labour force participation rates in New Zealand reduce rapidly beyond age 55 as many people aged 55-64 leave the workforce. The Welfare Working Group reported that when people older than 50 become unemployed they are likely to remain unemployed for a long time. At the same time many people remain in work beyond age 65, so universal superannuation eligibility at 65 seems arbitrary.

While there are many unemployed now, if economic recovery progresses as we hope, there will be labour shortages again. Our productivity and economy will benefit, along with the cost of funding unemployment and retirement, if we can keep older people productive. To do that we need to turn around the attitude that work is bad and retirement is good. Continuing to work provides people with a sense of meaning and purpose. Staying engaged in the workforce is stimulating intellectually, socially or physically and likely to benefit the health of older workers. Various researchers have concluded that choosing when to retire is a crucial factor for higher wellbeing in retirement.

Assessing the option of introducing compulsory superannuation is a worthwhile step because there should be stronger incentives for saving. But the conversation should not end there because important issues remain. How will universal superannuation be changed to ensure it is fiscally sustainable? How will retraining, employment and retirement policies ensure people are encouraged and equipped to continue working, when that is in everyone's best interests?

We need a solution that promotes employment and provides adequate retirement incomes for older people while growing capital for productive investment and reducing the fiscal exposure of future generations. The sooner that solution is in place the sooner we can get the benefits.