Productivity Commission

Commonwealth Government of Australian

Friday 9th September, 2016

Dear Sir/Madam,

Women in Super Submission to the Productivity Commission on How to Assess the Competitiveness and Efficiency of the Superannuation System

Women in Super welcomes the opportunity to comment in relation to the report on the competitiveness and efficiency of the superannuation system.

About us

Women in Super (WIS) is a national advocacy and networking group for women employed in the superannuation and financial services industries.

WIS advocates on behalf of its members and women generally to improve women's participation in the workforce and therefore their retirement prospects and access to superannuation.

WIS provides education and support to assist women in gaining opportunities to develop broader business, professional and personal networks, and aims to educate the greater community in order to improve their knowledge of superannuation. WIS strongly supports and encourages the appointment of women to superannuation fund boards, and works with other organisations and stakeholders to achieve this.

Women's Retirement Outcomes

It is well known that the current superannuation system that has been in place since the 1990s cannot be said to be efficiently meeting the needs of half the population of Australia – namely women. The average woman in Australia currently retires with almost half the superannuation account balance of the average man and this is unlikely to change in the near (or indeed longer term) future under current policy settings.

These facts are well known and should be acknowledged by the Productivity Commission and influence the scope and work of the Commission in assessing the competitiveness and efficiency of the superannuation system.

Given their lower level of superannuation savings women are more likely to be reliant on the full or part Age Pension. The interrelationship between the Age Pension and superannuation is of critical importance to women and should be considered with respect to the system fairly and efficiently enabling women to enjoy a dignified retirement with adequate income. The Productivity Commission should examine the interrelationship between the Age Pension and superannuation.

The Report of the Senate Economic References Committee Inquiry into economic security for women in retirement recommended that all government policy analysis in relation to retirement incomes include specific analysis comparing the impact of each proposal on men and women[1].

Women in Super recommend that the Productivity commission wherever possible collect and analyse data for men and women to ensure that the Commission can identify any differential impacts of the operation of the system and potential gender impacts of any changes to the system. As a minimum the Commission should have a stated objective of ensuring that changes do not further disadvantage women.

Commentary below with respect to measuring the competitiveness and efficiency of the system serves to illustrate potential impacts related to the different attitudes and behaviours of men and women.

Chapter 4 What are the objectives of the superannuation system?

In light of the huge and persistent differential between superannuation outcomes for men and women and the inevitable outcome of poverty in retirement for many women, Women in Super does not support the overarching objective suggested by the FSI and now released by the Government in draft legislation. The proposed objective does not address adequacy or outcomes for women.

Women in Super support an objective which includes statements regarding;

- *the right to a 'dignified' retirement;*
- *the standard of living we expect in retirement;*
- *the relationship between superannuation and public pensions to achieve the desired income; and*
- *specific reference to 'all women and men'*[2].

Women in Super also propose the adoption of 'supporting objectives' as detailed below. WIS is concerned that the 'system' objectives suggested by the Productivity Commission to test the efficiency and competitiveness of the system should not undermine these supporting objectives.

"The supporting objectives of superannuation should be founded on the principles of certainty, adequacy, fairness, sustainability, stability and equity. These include the recognition of the interrelationship between the Age Pension and other compulsory and voluntary methods of superannuation savings; the balancing of needs between the different generations of Australians the understanding that men and women have different working lives and patterns; and the recognition

[1] Report 'A husband is not a retirement plan' - Achieving economic security for women in retirement. Overview and list of recommendations, Recommendation 15, paragraph 6.95, Commonwealth Government of Australia, 29 April 2016

[2] Women in Super Submission to the Commonwealth Government on the Objective of Superannuation, 6 April 2016, pg. 2

that it is the shared responsibility of all stakeholders to deliver a Retirement Income System that benefits all Australians – men and women.[3]"

Chapter 5 Assessing competitiveness

Member Engagement

We agree that the Australian superannuation system has some unique features and therefore a somewhat customised approach is required of the commonly used frameworks for assessing competition. However, the Issues Paper states that 'a key aspect of assessing the underlying conditions for competition relates to concerns that disengaged and uninformed members are not generating competitive pressure on supply.'

We agree that member engagement can be a partial and (at times) misleading indicator of efficient competition. By its very nature superannuation is a long-term investment and if members are confident that they are with a trusted superannuation supplier then the level of engagement may indeed be low so this by itself does not indicate that the member is dissatisfied or that there is any need for them to change superannuation providers. Nor is this necessarily a reason for concern or a reason for assuming that there is a lack of pressure being exerted on competition.

We believe the best way to assess the efficiency of the system is to measure the level of retirement income the superannuation system is delivering to members and benchmark this against an adequate level of retirement income.

Putting a gender lens over a robust assessment of actual retirement incomes and adequate retirement incomes is one clear way of establishing whether the system is meeting its objectives.

Measuring behaviours like switching activity indicate engagement but do not have a bearing on outcomes. At best they can be a distraction and at worst they establish a framework for superannuation providers to claim that they are 'meeting members' preferences' even if they are delivering lower returns.

It is also well known that higher levels of engagement occur when markets are volatile and investment performance falls and there can be higher activity levels such as switching from international to domestic equities, from equities to bonds, from bonds to cash etc. or switching from one provider to another. Such moves are often motivated by fear and a lack of understanding of the long-term nature and risk profile of investments and indeed of financial markets so not all such switches are beneficial to members.

Life stages often coincide with a need for greater information and therefore higher engagement levels – marriage, parenthood, divorce, death of a partner - or factors such as - financial hardship, instances of domestic violence, receipt of inheritance or substantial sum of money that might trigger a re-

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[3] Women in Super Submission to the Commonwealth Government on the Objective of Superannuation, 6 April 2016, pg. 3

evaluation of strategy. A particularly important time from the perspective of requiring further information is as a member approaches retirement.

One could infer therefore that lower levels of engagement are to be expected when markets are not facing substantial volatility and investment performance is on track or increasing year on year.

Financial Literacy

Assessing the competitiveness and efficiency of the system through including assessments of levels of financial literacy are not necessarily a great indicator of member engagement nor that the system is meeting its objectives and delivering adequate retirement outcomes.

It is widely acknowledged that improvements can be made to levels of financial literacy around the country however, without a concerted effort to educate the general public about superannuation whether that is by introducing programs in schools and universities; workplaces; focusing on the self-employed and others not in the superannuation system (such as those not meeting the $450 monthly threshold) and those from culturally and linguistically diverse backgrounds who may not have any familiarity with superannuation) this is unlikely to be achieved. The public already has access to online tools and calculators through the ASIC MoneySmart website and websites of superannuation providers.

Research has shown that generally women will understate their levels of financial literacy and men will overstate theirs. This should be borne in mind if and when surveys are used as a method of gauging levels of financial literacy to assess competitiveness.

The Swedish Example – Default and Choice in Member Engagement

Assuming that 'default' is an indicator of lack of member engagement can in fact be erroneous as demonstrated by recent studies into the Swedish pension fund system where large amounts of money are managed in the default account (PPM) of the Seventh Swedish National Pension Fund (AP7).

In the 1990s Sweden, like Australia, undertook a major overhaul of its pension system and in 2000 launched the current system made up of four active choice funds and one default fund (AP7).

The design of the Swedish system is interesting from an Australian system as it is public and mandatory covering the entire workforce (4.4 million individuals). Secondly, the number of investment opportunities in the Swedish system is large and individuals can choose between investing with one or up to five funds and between them the funds offer more than 460 equity, fixed-income and mixed funds product offerings. Thirdly, in addition to the afore-mentioned funds, the government provides a publicly managed mutual fund that serves as a default alternative for individuals who do not make an active investment decision (namely AP7). Fourthly, the Swedish default alternative is associated with a high risk since it mainly consists of equity holdings so it is not the low risk option traditionally associated with members who typically choose or end up in the default option in other countries (e.g. 401 (k) plan in the US which is fixed income based or even the balanced option which has become the default option of many Australian superannuation providers).

Once individuals make their choices in many cases they are likely to stick with them and not change them. This is not a failing of the system but rather an assumption that at the time of decision making many individuals do indeed seek advice (perhaps not formally from financial planners but from superannuation websites, peers and colleagues) and once comfortable they make a choice. Superannuation savings are for the long-term so short-term trading and multiple changes should be discouraged unless there is good reason. There are inherent costs associated with changing investment choices and changing fund providers.

A study undertaken in Sweden post the allocation of first round funds to the Swedish pension fund system, found that those who had prior experience in financial markets and were married were substantially likely to make an active choice in their first round of decision making. Next in line were advanced education, higher income and female gender also made individuals more likely to make an active choice.[4]

However, the Swedish experience shows that after the first flurry of choice, participants drop off and are not so keen to actively choose. This may be due to the increasingly large number of funds available (too overwhelming for some), a lack of encouragement (no widespread media and marketing campaigns encouraging choice), younger entrants to the market (a longer time frame to retirement so less interest in what happens to their money now) and lack of enthusiasm (the Global Financial Crisis and lower performance returns can lead to a lack of interest).

Perhaps it is also a sign of the increase in popularity of the Swedish default fund and this may well be a final factor that may have contributed to the decline in active choice. So, selection of the default fund is in many ways a recognition by many Swedes that it is in fact a good investment choice. It has been widely perceived as a 'safe choice' and one that has been consistently well-managed (high rate of retention of employees, highly regarded CEO) and is a low-cost alternative (level of fees are mandated) to other funds. Furthermore, the default fund has outperformed the weighted average of actively placed funds in recent years, which may further have increased the attraction of non-choice.

All the more interesting as the Swedish government enacted some rules to make it harder to invest in the default fund. Individuals cannot actively opt for this default fund – they are only invested in it if they make no active choice. Furthermore, it cannot be marketed to potential "customers". However, costs are kept low through automation, bulk trading of fund switches, low levels of employees administering the plan and once-a-year transfer of funds into accounts.

It is also worth noting that fewer than 6% of all premium pension savers in Sweden made even a single fund switch in 2004. Only a little over 600 account holders out of more than 5.3 million were very

[4] "Which Individuals Make Active Investment Decisions in the New Swedish Pension System?" Stefan Engstrom, Stockholm School of Economics & Anna Westerberg, National Social Insurance Board, Sweden, unpublished paper, September 16, 2003 & "Design and Implementation Issues in Swedish Individual Pension Accounts", R. Kent Weaver, Professor of Public Policy and Government, Georgetown University, Center for Retirement Research, Boston College, April 2005

frequent traders, defined as undertaking more than twenty fund switches during the year, while two-thirds of those who switched funds did so only once.[5]

Despite such a concerted and large scale educational and marketing campaign by both the government and the funds involved regarding the different investments options and what they meant 67% made an active choice and 33% made no choice and ended up in the default option.[6]

SMSFs – Joint or Multiple Trustees and Women

A recent study conducted by the Commonwealth Bank of Australia and the SMSF Association[7] highlights the need for financial advisors and SMSF members to consider the often significant differences that exist between trustees of different ages and genders when building their SMSF portfolio.

Women currently make up 47% of all SMSF members and the above mentioned study concluded that there were differences in behaviours, confidence and market outlook among males and females. Overall women indicated that they were less confident than men in their understanding of all asset classes and that men were more likely to be the sole decision maker in a joint trustee scenario.

According to the research, SMSFs with more than one member make up 72% of all SMSFs, where SMSFs have two members, the most common is spouses/partners (88%). Among SMSFs with multiple trustees, men (65%) are significantly more likely than women (28%) to be the sole main decision maker for their SMSF. Less than half (49%) of SMSF trustees were very confident that following a separation or divorce and their partner ceasing to be a trustee that they would have sufficient knowledge to take over sole responsibility for managing their SMSF investments. After separation, divorce or death of a co-trustee, women (41%) are more likely to make changes to their SMSF in line with their own investment goals while men are more likely to maintain the strategies already in place (53%)[8].

Given the above, we should analyse the ease with which can exit from SMSFs and enter the institutional super market if that is what they wish to do post separation, divorce or death of their partner especially where that partner was the main decision maker.

Furthermore, we should be assessing whether the needs are being met of all trustees in assessing the efficiency of the superannuation system? What if both spouses have different investment horizons and risk tolerances? Are superannuation providers documenting at the outset and revisiting periodically retirement goals with both spouses?

If the needs of all trustees ae not being met, then can a trustee exit with ease from SMSFs and move to another structure? This has major implications when parties wish to separate assets due to separation,

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[5] "Social Security Smorgasbord? Lessons from Sweden's Individual Pension Accounts", R. Kent Weaver, Professor of Public Policy and Government, Georgetown University, June 2005.
[6] S. Engstrom and A. Westerberg (see footnote 4 above)
[7] "Women and SMSFs - Empowering and supporting SMSF members on their investment journey - A study of Self Managed Super Funds (SMSFs)", Commonwealth Bank of Australia and the SMSF Association, February 2016
[8] Ditto

divorce, cases of family violence or even following the death of their partner especially where that partner was the main decision maker?

Chapter 6 Assessing Efficiency

Assessing Investment Performance

We would like to see 'gender' included in any assessment of the investment strategies or investment decision making process of members. There are numerous studies available that show that men generally believe they possess superior investment ability and that they can beat the market and men's overconfidence leads to excessive trading which can cause underperformance[9].

Recent research in Australia appears to bear this out. In a recent study by the Commonwealth Bank of Australia and the SMSF Association in February 2016, men cited they are more likely than women to set up their own SMSF to gain more control over their investments (55% compared to 45%), to be able to choose specific shares to invest in (23% compared to 15%) and because they believe they can make better investments than super fund managers (19% compared with 13%). Women currently make up 47% of all SMSF members and the above mentioned study concluded that there were differences in behaviours, confidence and market outlook among males and females. Overall women indicated that they were less confident than men in their understanding of all asset classes and that men were more likely to be the sole decision maker in a joint trustee scenario.

However, other studies show that gender impacts investment behaviour and the approach of men and women is different leading to misunderstandings in interpreting the behaviours. There are three main ways in which gender differences in investment behaviour manifests itself[10]: (i) women tend to focus more on longer-term, non-monetary goals**.** Women generally associate money with security, independence and the quality of their and their families' lives[11]. (ii) Women tend to be thorough and take more time to make decisions than men and (iii) women seek help more, not relying solely on their own knowledge. Taking longer, more calculated decisions and seeking information from numerous sources is not in fact to be interpreted as lacking in confidence or understanding but rather careful research and validation of what are essentially life-long decisions.

In an excellent report put together in 2015 by Fidelity Investments entitled "Maximizing a Major Opportunity: Engaging Female Clients: A Guide to Engagement", the authors highlight how women are a growing market for superannuation and financial products but that in order for them to be engaged and retained by organisations there is a need to first understand the attributes that make them

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[9] "Boys will be boys: Gender, Overconfidence, and Common Stock Investment", Brad M. Barber and Terrance Odean, © 2001 by the President and Fellows of Harvard College and the Massachusetts Institute of Technology, The Quarterly Journal of Economics, February 2001

[10] The Blackrock Blog article by Nelli Oster, Investment Strategist and PhD in Finance, Stanford Graduate School of Business

[11] "Maximizing a Major Opportunity: Engaging Female Clients A Guide to Client Engagement", Fidelity Investments, 2015 https://fiiscontent.fidelity.com/954113.pdf

uniquely different from male clients. They contend that there are five key differences in how women and men communicate, relate interpersonally, learn, are hardwired, and view wealth[12].

There are other nuances too such as females tend to be more atune to debates over domestic, ethical and environmental investment practices and often choose their investments on the basis of the 'greener' option and this is especially true when higher educated.

Conclusion

Women in Super understands that it is not within the scope of this review to address current policy settings including the taxation of superannuation which results in considerable inequities, that contributes to the gender super gap, or suggest policy settings that may alleviate the gender super gap.

However, when assessing the competitiveness and efficiency of the system through establishing indicators that measure the level of competition and efficiency in the superannuation system, there is room within those indicators to include gender and therefore assess whether the system really is addressing the needs of all members, male and female given what we know about gender differences in financial behaviour.

Furthermore, Women in Super would like to see the overarching objective of superannuation and its supporting objectives address adequacy or outcomes for women as we do not wish to see the 'system' objectives suggested by the Productivity Commission to test the efficiency and competitiveness of the system undermine these supporting objectives.

Contact

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[12] "Maximizing a Major Opportunity: Engaging Female Clients A Guide to Client Engagement, Fidelity Investments", 2015 https://fiiscontent.fidelity.com/954113.pdf