

## Abstracts

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### **Population Ageing and Retirement Income in Australia**      **John McCormack**

While significant changes to the Australian retirement income system have been underway since the mid-eighties, mainly in response to population ageing and essentially to encourage greater self-provision, the recent election of a national conservative government has coincided with a renewed analysis of the impact of this demographic transition. The new government established a National Commission of Audit to review and recommend medium and long-term improvement in Commonwealth finances. The report of the Commission specifically highlighted population ageing, aged health care, public aged pension expenditures and the need for intergenerational fairness as Budget pressures requiring action to moderate expectations about what the Commonwealth government could be expected to provide in the future. The selection of recent Australian journal articles reviewed below provides some commentary on these issues as well as some technical aspects of retirement income changes and their impact on different groups.

Paul Johnson. 1996. Grey horizons: who pays for old age in the 21st century? *Australian Economic Review*, 3, 261–271.

Paul Johnson, from the London School of Economics, was in 1996 the Richard Downing Fellow in Social Economics at the University of Melbourne, Australia, and this article is a revised version of the annual Downing Lecture. Johnson was surprised at the level of media interest and commentary on the implications of population ageing in Australia, which however provided a perfect opportunity to analyse the underlying assumptions. He unpicks both demographic and economic assumptions to argue that these pessimistic interpretations of the ‘old age crisis’ result from a narrow reading of the demographic data, and that the changes in age structure will be no greater than those already experienced and accommodated this century. He shows, for example, that although the total dependency ratio in Australia is currently 50 people per 100 aged 15–64 years, and that this will increase sharply to 55 in 2021 and to 65 in 2041, this level is not new for Australia, for in 1901 the total dependency ratio was also 65.

He does point out, however, that the composition of this ratio will be quite different in 2041, with a large aged dependency share (36:29), compared to 1901 where the young dependency component was the largest (58:7). Thus Johnson does not deny that there could be some problems with future pension

financing but argues that they require political decision-making rather than particular technical economic solutions or a shift from public to private finance, as argued by The World Bank in its recent report, *Averting the Old Age Crisis*. Johnson discusses options such as reducing the indexation of pensions, but he believes the preferred solution is to 'encourage' current workers to defer consumption in favour of savings through compulsory higher superannuation contributions – as is currently under way in Australia with the implementation of the Superannuation Guarantee Act 1991.

David Knox. 1996. Contemporary issues in the ongoing reform of the Australian retirement income system. *Australian Economic Review*, 2, 199–210.

David Knox is a Professor of Actuarial Studies who has written extensively on the retirement income system in Australia. In this article he critically examines recent Budget changes to employees' contributions and argues for a more integrated public and private scheme to ensure fairness and affordability. He applauds The World Bank Report's three-pillar model of retirement income and points out that risk diversification is essential because of the projected size of the Australian superannuation fund. The assets will grow from 42% of GDP currently to 74% by 2030. This compares with 1991 estimates for the United Kingdom and United States of 51% and 60% of GDP respectively.

Although Australia has now established a three-pillar structure, Knox questions whether the compulsory superannuation component will be adequate. Recent budget changes introduced a compulsory 3% employee contribution matched by an income-tested 3% government contribution, in addition to the current employer's 9% of earnings by 2002. Comparing underlying assumptions about a 40 year working life with the observed diversification of employment patterns, and the volatility of investment returns in defined contribution systems, leads him to suggest an alternative refundable rebate system for employee contributions. For example, employees would receive, say, a 25% rebate on the first \$2,000 of contributions that year plus a sliding scale for further contributions. A revised tax system would provide less incentive for high income earners who already save more, and a more progressive tax on lump sums. He then argues that the superannuation pillar and the public assistance age pension must also be more integrated as they currently differ in three ways: on form – one is predominantly a lump sum whereas the other is pension only; on age eligibility – one is currently preserved to 55 years whereas the other is to 65; and on income measures – one is based on lifetime income whereas the other is a flat-rate benefit. He recommends a taxable universal pension from age 65 years, associated with increased tax on larger superannuation benefits. He believes this will provide a better spread of retirement income and risk across the three pillars and greater equity between the generations.

Diana Olsberg. 1994. Still missing out: women, superannuation and retirement income. *Just Policy*, 1, November, 45–49.

Diana Olsberg is the Executive Director of the Australian Superannuation Trustees and in this article she provides an expert view on the impact of retirement income changes for women. She begins by tracing the history of superannuation in Australia, pointing out that, until the 1990s, coverage was very limited and favoured full-time workers in large or civil service organisations. While the recent compulsory superannuation system will rectify coverage, she foresees long-term difficulties for women based on their broken employment and low levels of lifetime income. She reports that women currently spend 17 years in paid employment compared to 39 years for men, although younger cohorts of women are substantially increasing their years in the work-force. She looks at the relative disparity in average fund assets, which show that, at retirement, men have assets in the range \$50,000 to \$70,000, while for women it is less than half – \$21,000 to \$30,000. She then analyses the work experiences of women revealing around nine interruptions due to maternity leave and to periods of child care, elder care, partner care, grandchild care and relocation due to husband's job mobility. She believes industry and occupational sex segmentation adds to this pattern through a greater propensity to be in part-time and casual work. She then discusses the gloomy situation of women who spend no time in the paid work-force, which leads her to conclude that the flat-rate public-assistance age pension is likely to provide the backbone of retirement income for many women well into the next century.

#### COMMENT

Australia has been characterised as a “wage earners’ welfare state” in which social protection was provided through institutional structures such as centralised wage setting, rather than through a comprehensive social security system. The recent superannuation reform, based on workplace earnings, can clearly be seen as an extension of this occupational welfare model. While it is aimed at improving the living standards of older people, it is also undoubtedly driven by the challenge of population ageing. With employers mandated to make the greatest share of contributions, however, savings on welfare expenditure should enable the means-tested public age pension to remain indexed and to serve as the backbone of retirement income while the new system financially matures. This scenario represents the position of the reviewed authors: they all to some extent argue against apocalyptic reactions to population ageing.

The latest figures from the Australian Bureau of Statistics (November 1995) show that the new system has achieved some impressive gains. Superannuation coverage of the employed is now 81 %, up from 32 % in 1974. Among full-time workers it is 87 %, and for part-time workers it is 62 %, up from 44 % in 1991. Also, the gender gap is narrowing with coverage extending to 82 % of employed males and 79 % of employed females. However, as Knox and

Olsberg point out, there is still considerable diversity across other dimensions of this retirement income transition to an older Australia. Industry differences are quite marked in terms of coverage with agriculture, where older workers are over-represented, recording the lowest coverage (50%). Similarly, employers and the self-employed have considerably lower coverage than employees. Also, the substantial number of working-age people not in employment, *i.e.* those unemployed or out of the labour force, are four times more likely not to have superannuation coverage.

Thus, as these authors have identified, while there have been positive changes in the Australian retirement income system, many issues remain to be dealt with to ensure adequate social protection not only for the current older population but also the impending baby-boom population bulge. While there is criticism of the residual nature of the social security system in Australia, it is nevertheless a secure safety-net for old people. Also, its low replacement rate pensions and benefits are offset somewhat by other factors in the economy, such as high rates of home ownership, a nationalised health system, and the increasing labour-force participation of women. The dilemma raised by Johnson and others about saving for retirement *versus* the need for current consumption, particularly among families with young dependants, has also been addressed to some extent by the introduction of a range of new benefits, such as additional family payments which focus on the needs of low income families. It is these complementary provisions, as well as the continuing changes to the retirement income system, that one hopes will enable all Australians to continue to live decently throughout their years.

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