

# Spending the savings

**KiwiSaver products and practices  
- the challenges and problems**

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## Spending the savings

▲ “How can middle-income retirees **best use** their savings for what might be a very long or very short retirement”

▲ “There are **virtually no** products that **do not** carry the risk of outliving capital”

**Why do we think that we need a product?**

yet individuals and society have a vested interest in facilitating this process”

Source: Symposium briefing notes

# Conclusions

- It is unlikely that a suitable third-party product could ever be developed that is “fair” to retirees and taxpayers.

- The pricing of the current system is not a return to a fair market value.

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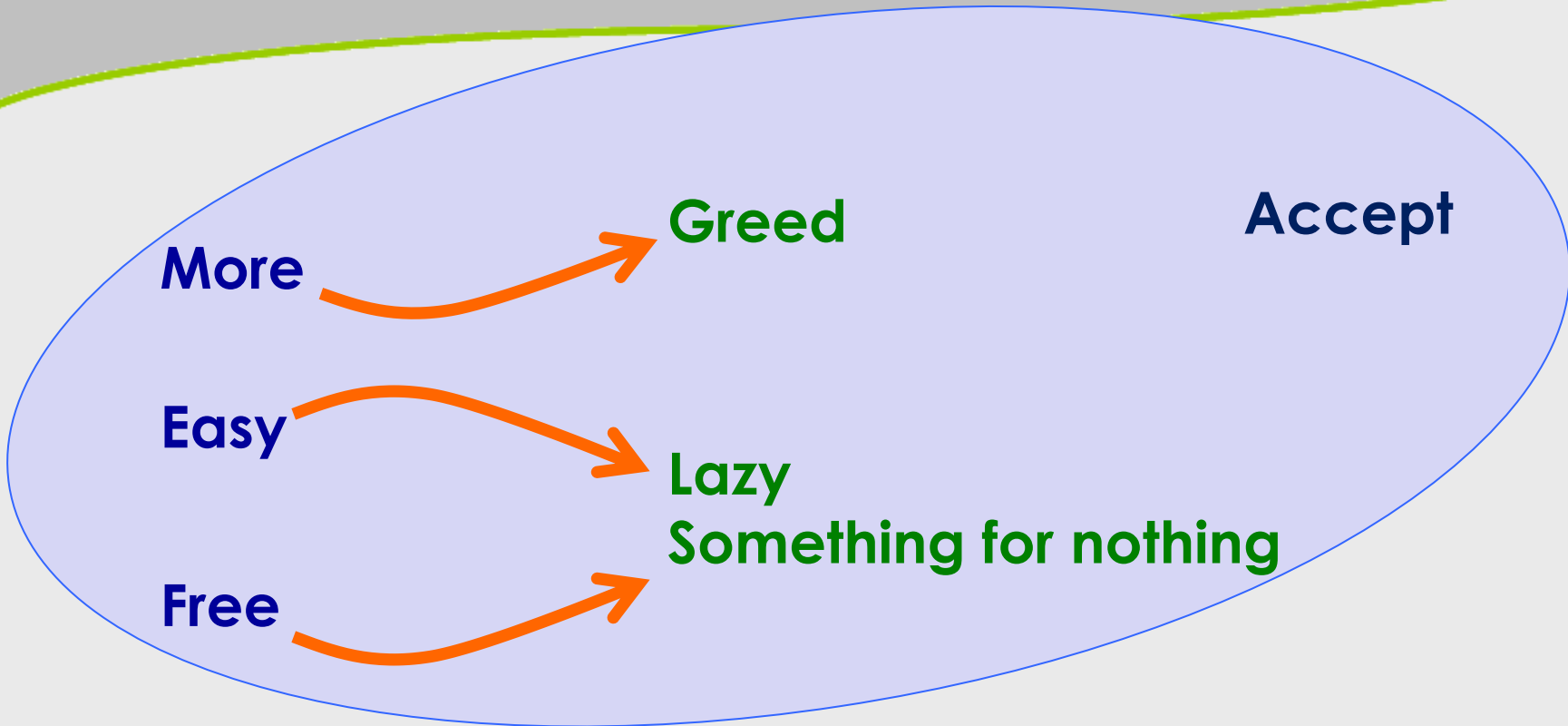
**The answer is a retiree centric service and facility, which combines a flexible low cost, transparent vehicle with clear and frequent information and education.**

Costs are prohibitive  
per as it is, what benefits do  
payers and society get?

# The basic problem

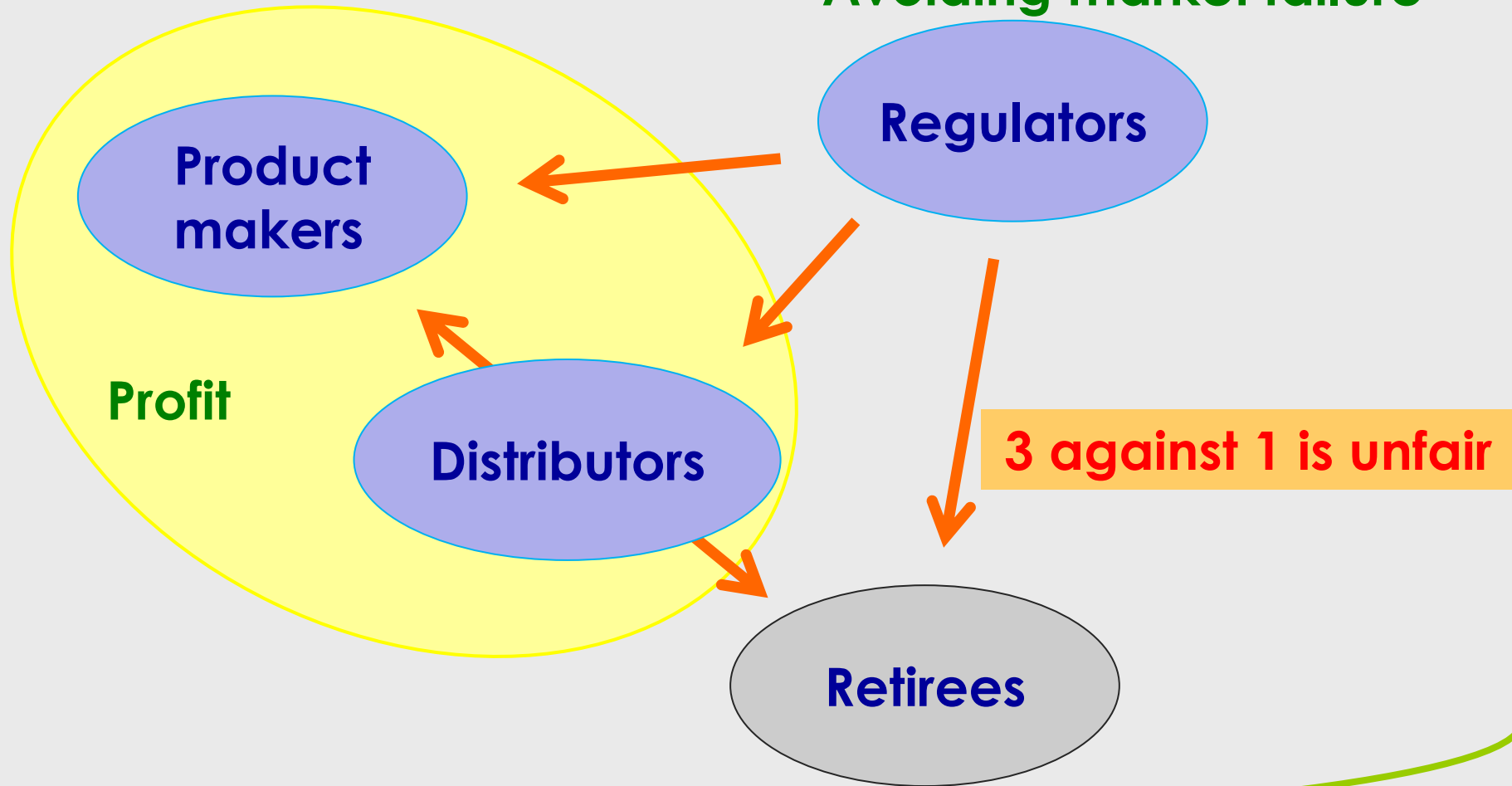
- ▲ Human nature
- ▲ Asymmetric information
- ▲ (Lack of ) competition
  - High cost of change
  - Sold not bought – relationship (/distribution)
- ▲ Conflicting stakeholder objectives
  - Regulators vs manufacturers vs distributors vs buyers
- ▲ Pricing of risk & unknowns
- ▲ It's a long time

# Human nature



# Tug of war

## Avoiding market failure



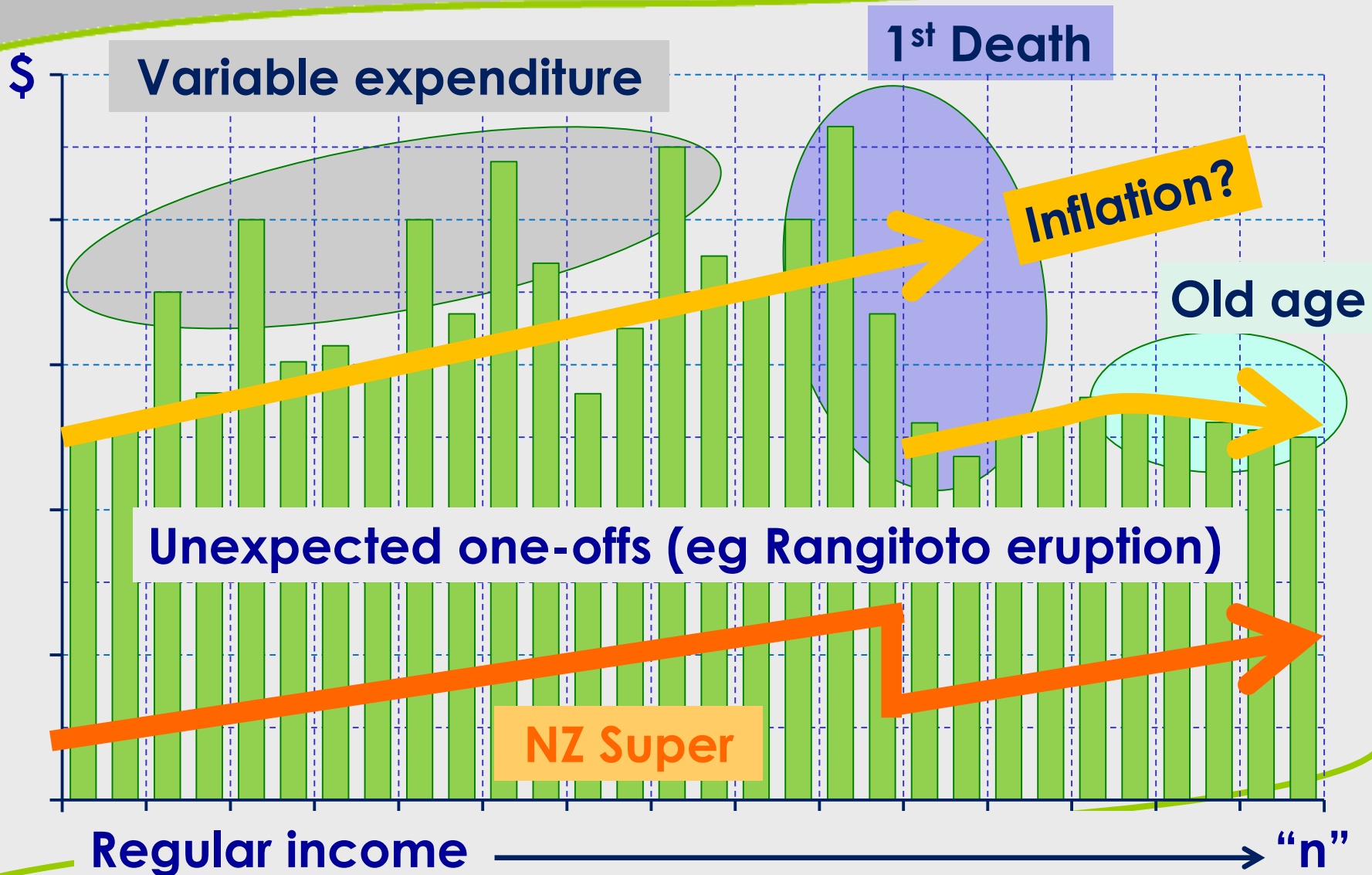
Income after tax and costs  
that matches expenditure

# Asymmetric information

- ▲ **Supplier knowledge advantage**
  - Retirees believe that there are “experts”
- ▲ **Buyer uninterested (or not main focus)**
- ▲ **Short-termism**
  - Can't think beyond immediate future
- ▲ **Complexity & risk**

**The world is  
against the  
individual buyer**

# Expenditure cash flow pattern





# Understanding the unknowns

## ▲ Expenditure cash flows

- Income, lump sums, unexpected events

## ▲ Inflation

## ▲ Duration (life expectancy)

- Longevity - medical advancements
- Age you lose your “marbles”

## ▲ Investment returns

- Average, pattern, income/growth split
- Tax, management fees, costs

## ▲ Country/city of final retirement

# Understanding the unknowns

## ▲ Support

- Advice, education
- Capability

## ▲ Legislative change

- Regulation
- Compliance costs
- Tax

## ▲ Product provider survival

- Market share, economies of scale

# Market behaviour

The portfolio approach to investing  
doesn't work in retirement



# Buyers get what is left

Strategy, markets, manager decisions



## Gross investment return

- Cost of regulation (hard & soft)
- Tax (& tax compliance)
- Cost of manufacturing
- Cost of distribution
- Industry profit
- Cost of advice

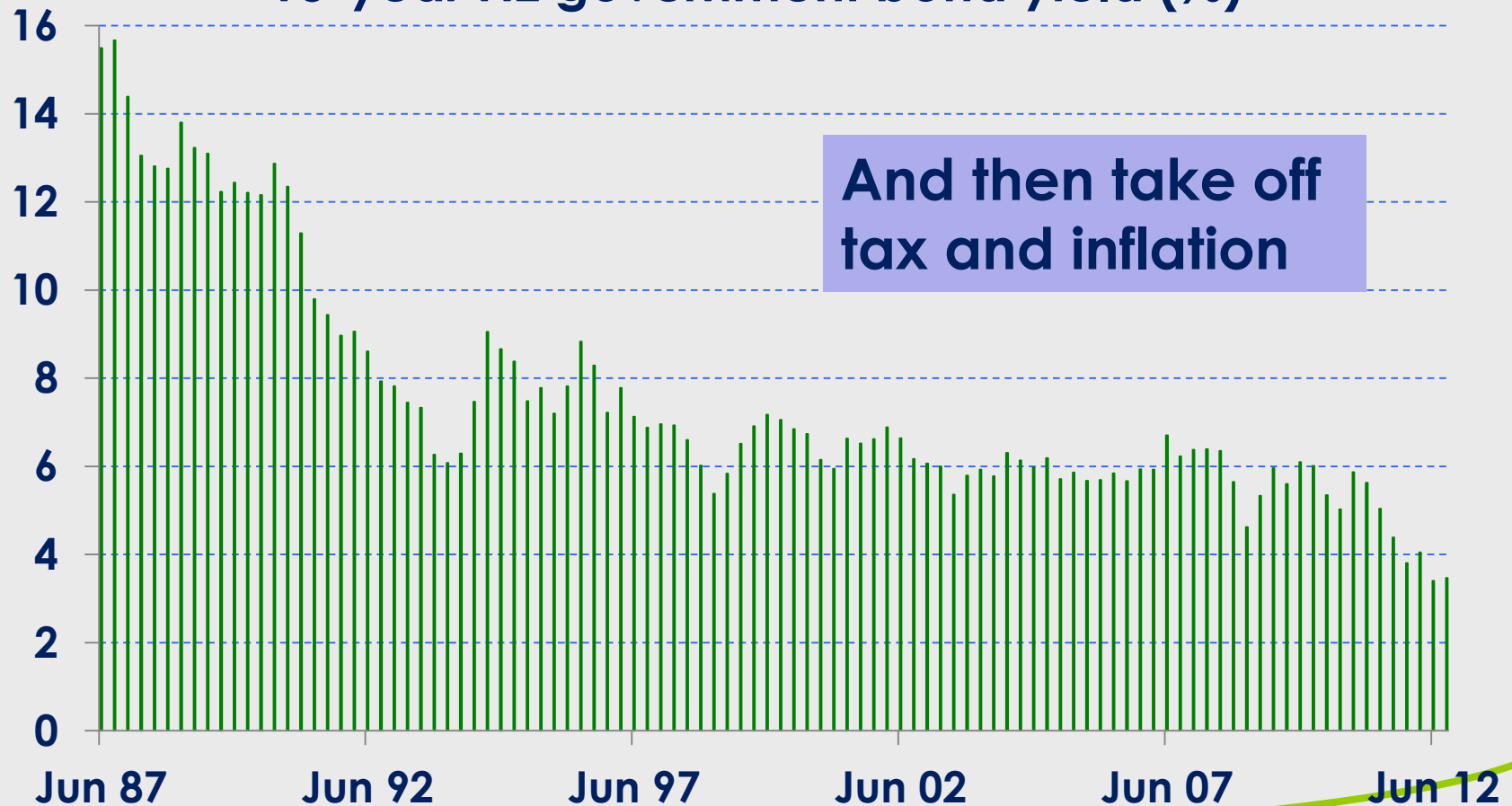
= Consumer outcome

Remember  
there will be  
extended  
periods of  
low returns

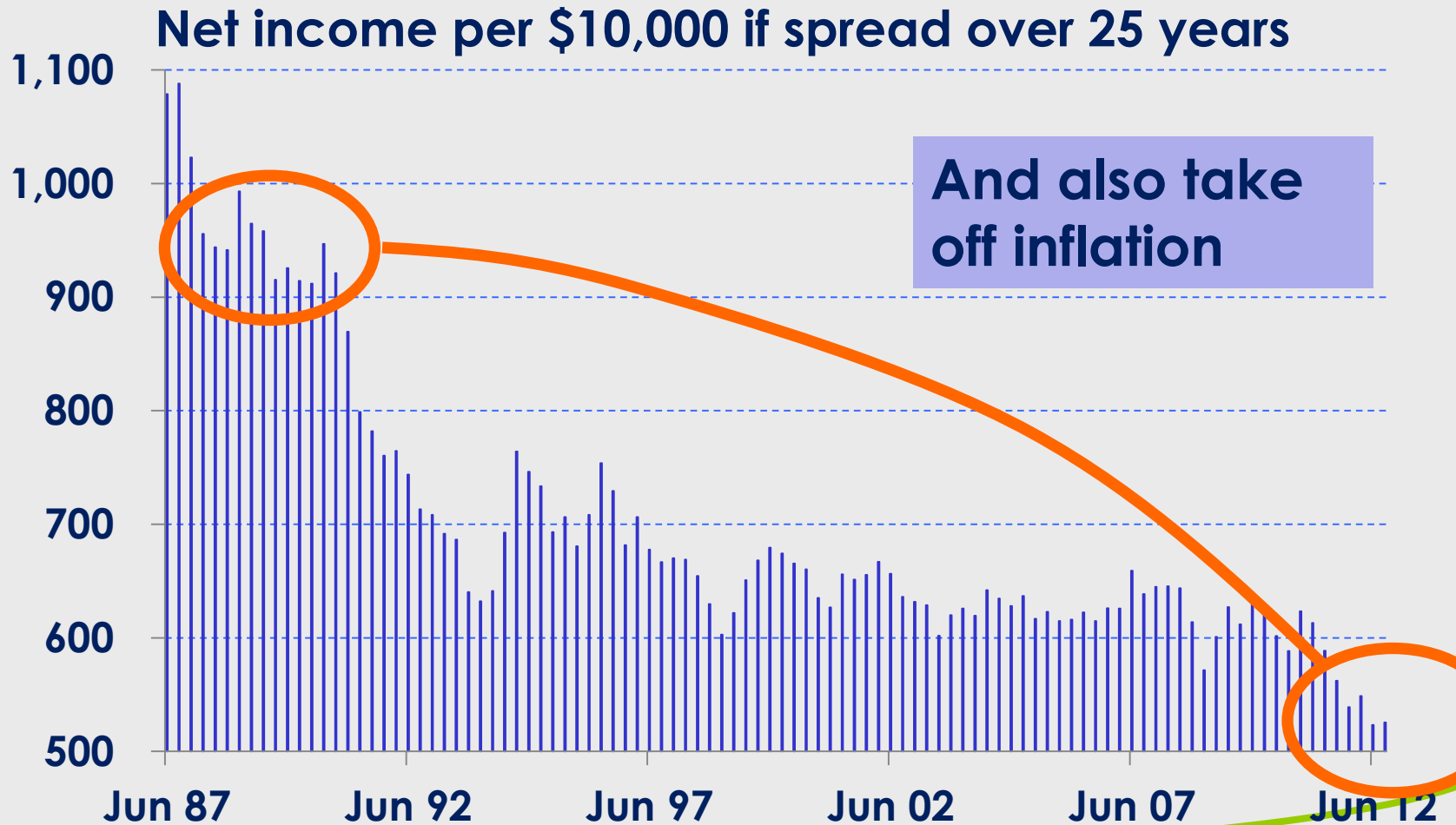
Total costs are too high  
to give a reasonable  
net return

# Returns vary a lot over 25 years

## 10-year NZ government bond yield (%)



# Resulting in a range of nominal incomes



# Pricing risk

**Profit**

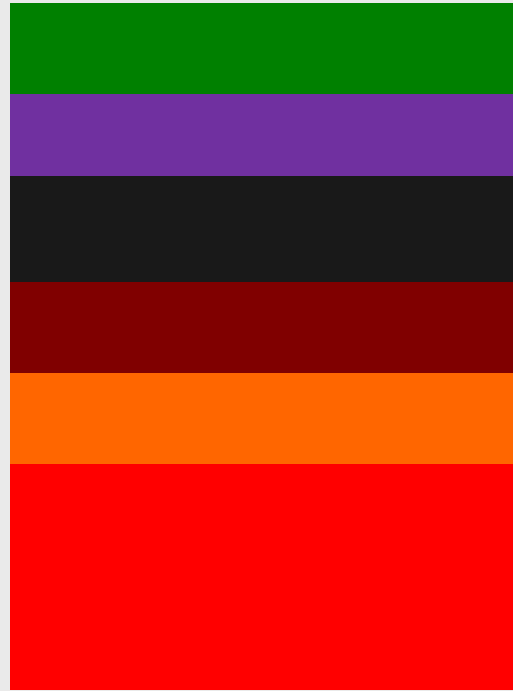
**Return on capital**

**Distribution costs**

**Administration costs**

**Statistical margin**

**Expected risk**



**The total margins and costs, price risk out of the market for most**

**Retirees are better to take on and manage their own risks at least in the early years**

# The role of government

## ▲ Reduce quantity & improve quality of regulation

- Adopt principles and not rules
- Ensure certainty & stability
- Adopt the sunlight golden rule

## ▲ Focus on standards of outcomes and not documentation of process (of inputs)

## ▲ Simplify the tax system

## ▲ Encourage risk management & not risk avoidance

**Take on longevity risk (?)**



# The solution



# Discussion



**"If something cannot go on forever, it will stop."**

**Economist, Herbert Stein**