Imagine a 15% world

Theo Marinis argues why the superannuation guarantee rate should be at least 15% and how this would benefit retirees.

By Theo Marinis

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Remember the good old days of defined benefit superannuation? You may not have realised it, but in order to generate around 70 per cent of your final pay after a 35-year career, your employer had to put away as much as 17 per cent of your income – over your entire working life.

Now there is a concerted push to stop Australia from increasing its compulsory level of contributions for all workers – the superannuation guarantee (SG) from 9.5 per cent to 12 per cent. This is dumb thinking – we should be pushing for 15 per cent, at least.

Some simple illustrations for my argument in favour of SG at the rate of 15 per cent versus 10 per cent over a 35-year career:

Let's imagine a person earns $80,000 and only has the SG (and to keep the illustration simple, never gets a pay rise and there is no inflation). Without the benefit of compounding interest, an annual contribution of $8,000 or 10 per cent of salary over 35 years would produce $280,000 in super. A contribution of 15 per cent per annum would produce $420,000.

If we compound these contributions by say 7.5 per cent (which is what happens in real life) over 35 years, an annual contribution of 10 per cent of wages would accumulate to $722,562. A contribution of 15 per cent would produce $1,234,000 – a difference at retirement of $511,438 (or $371,438 after taking into account foregone income of $140,000 – $4,000 per year over 35 years).

Clearly, the recipients of a 15 per cent SG contribution are much better off

financially at the end of their career.

The problem was, as Paul Keating and Bill Kelty recognised in the early 1980s, very few people other than politicians, public servants, bankers and insurance workers received this wonderful payment for life In fact it is estimated that at the time, more than 90 per cent of workers received 'squat', other than perhaps a watch and measly government pension (for a single pensioner this is currently $472 per week) and, as a result, a very basic sub-standard of living in retirement!

Fast forward to last year when Treasurer Josh Frydenberg set up a review to argue against the need for the mandated (already legislated) SG contribution increase from 9.5 per cent to 10 per cent from 1 July 2021. Subsequent increases will see this move to 12 per cent of employment income by July 2025; still well below the 15.4 per cent super contribution to which Australian politicians are entitled, now.

The nub of the argument around SG is about consumption… now versus later.

It has become dogma for all involved in any discussion in respect of retirement policy. The forced nature of long-term saving generally goes against the grain for those nominally on the right of politics, whilst for many of those on the left, superannuation has been elevated to an almost religious position of infallibility.

The small business lobby often argues that the cost of super is too high and that workers cannot currently afford to forgo wages in lieu of increased payments to super.

These same arguments (or excuses) were also raised back in the late 1980s and early 1990s when the SG system was expanded for all and it morphed into the excellent super and retirement income system we have in Australia today – despite the claims of the critics.

Personally, I fall in the '15 per cent at a minimum' camp.

As an employer of around a dozen people, I believe that the cost is negligible when compared to the long-term emotional and intellectual benefits provided by having financial security. It is also my belief that in a macro-economic scenario, the short-term pain of foregone wages is well offset by the long-term benefits for society, the

federal budget, individuals and their families.

As someone who has had the good fortune to spend a lot of time with retirees, I have never heard one say, “I wish I had less money”.

Naturally, there are arguments about free choice, but the experiment of allowing people to save for themselves in retirement has been done – and it failed miserably over the last 5,000 years. If it is compulsory, it happens, if it’s not – it doesn’t!

We are still in the early days of super, which has really only been a ‘thing’ since the late 1980s. Whilst there are some of us at that time who were lucky enough to be employed straight from university (in my case in the Australian Public Service with 17 per cent of salary per annum paid into a government super scheme) there are plenty of people who have not benefited from super throughout their entire working lives.

Many who were born before 1970 may well still have to fall back on social security in later years, but the percentage of Australians doing that has dropped significantly – and the trajectory is speedily downward. That’s a great relief for future generations who will be saddled with the COVID-19 debt, but that’s a separate discussion.

Thanks to the approximate $3.0 trillion dollars we have invested in super, Australia is now a net exporter of capital. We are already seeing our large super funds investing globally in infrastructure, spreading our sovereign risk. That capital simply did not exist before super. It was consumed.

If we think about the retiree from a personal perspective, rather than a statistic (which is my preferred position) in the simplistic illustration above, based on an SG contribution of 15 per cent, that retiree will have a pool of $1,234,000. If drawn down at 5 per cent per annum this pool will provide an income of $61,700 per annum, tax-free. Based on an SG contribution of 10 per cent and the same rate of drawdown, the resulting pool of $722,562 will produce an annual income of just $36,128. I know what I would prefer.

The $25,500 per annum generated by the additional 5 per cent contribution to

super could translate to an annual overseas trip, better healthcare (i.e., including retaining private health insurance) a new car or a weekly trip to a great restaurant, wearing new clothes – or perhaps, a significant 'feel good' donation to a local church or charity.

The point is that with more wealth comes more choices (and perhaps, more dignity). From a micro-economic point of view, that's what I want from retirement.

From the macro-economic perspective, that extra spending by retirees now (thanks to not just subsisting on an age pension) is stimulatory for the economy. It has the multiplier effect of flowing revenue into business, salaries to employees, and GST and tax revenue for both state and federal governments – this was not possible in the 1980s!

Whilst the simplistic illustration such as the one above could never be real (no- one starts on a wage and finishes their career three and a half decades later earning the same, and inflation rates will vary) it does highlight the point that I want to make. Thanks to the compound effect, a little extra into super goes a long way!

The cynical reader may say "he's a financial adviser, so he has a direct vested interest in encouraging more super savings." I am happy to say that is not the case, as my advice fee (as with more of my peers, these days) is based on a fixed flat dollar fee or on hours worked, not on the size of a client portfolio.

Meanwhile, as the debate goes on in political circles, those of us outside the Canberra bubble should, perhaps, pay less attention to what the politicians say, and more attention to what they do – as they continue to pay themselves a 15.4 per cent per annum super contribution.

Australia is reputed to have the world's third-best superannuation/retirement income system. It is within our grasp to make ours the standard-bearer globally if we can just put aside these partisan debates.

I'll finish with a truism to reinforce the illustration above: "The way to get the best result from superannuation is to contribute as much as you can, as soon as you can – for as long as you can."

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