

## Chapter Six

### The Case for Change

#### Introduction

6.1 This chapter examines the economic arguments for encouraging a more progressive transition from work to retirement in Australia. Quite apart from the personal and family impacts of early and unplanned retirement noted in the previous chapter, a more progressive transition from work to retirement in Australia would help redress the gap in funding of retirement and the resultant burden on the government, and improve Australia's economic growth and efficiency.

6.2 The Committee notes, however, evidence that the current under-employment of mature age workers and pressure on the government's retirement income support system may be addressed in the future simply by labour force pressure for mature age workers to remain in the workforce as the absolute numbers of workers declines.

#### The gap in retirement funding

6.3 During the inquiry, various parties argued that a more progressive transition from work to retirement in Australia would go some way to addressing the current gap in private funding of retirement. The fundamental determinants of retirement incomes are the capacity for workers to earn income and save, together with the length of time that retirees spend out of the workforce.

6.4 In this regard, the ABA argued in its written submission that if superannuation fund members could be encouraged to defer retirement beyond 65, there would be many fiscal advantages including longer time for contributions to accumulate, a reduced period of consumption in retirement and additional contributions to society through taxes and expenditure. For example, if a male aged 65 on average weekly earning was prepared (and able) to defer retirement for five years, the government would generate savings of nearly \$100,000 under existing rules.<sup>1</sup>

6.5 In its report *Superannuation and standards of living in retirement*, the Committee noted a high degree of consensus that the desirable income target for a retiree is a replacement rate of 70-80 per cent of pre-retirement expenditure (which equates to approximately 60-65 per cent of gross pre-retirement income), a target which would have to be higher for those on less than average weekly earnings, and lower for those on high incomes.

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1 *Submission 41, ABA, p. 7.*

6.6 At the same time, however, the Committee noted in *Superannuation and standards of living in retirement* that notwithstanding the substantial increase in superannuation coverage as the superannuation system in Australia matures, the majority of older Australians will still rely on the age pension for a significant part of their income.

6.7 The Committee notes in particular that most baby boomers have not had the benefit of a full working life under the compulsory superannuation system and, other savings aside, that their incomes in retirement are likely to fall well short of the consensus target level of 70-80 per cent of pre-retirement expenditure (approximately 60-65 per cent of gross pre-retirement income).

6.8 In its written submission, FaCS indicated that by 2050, with a fully mature superannuation system, it is expected that 75 per cent of people aged 65 or over will still receive the age pension. Of those receiving the age pension, only one-third will receive the full rate. Currently, two-thirds of people receiving the age pension receive the full rate.<sup>2</sup>

6.9 Table 6.1 below shows projected Commonwealth spending on payments to individuals, including age and service pensions, from 2001-02 to 2041-42. The table shows a large increase in expenditure on the age and service pension which reflects the ageing of the population. This is despite the expected decline in the eligibility for the age and service pension in the future due to the maturing of the superannuation system.<sup>3</sup>

**Table 6.1: Projected Commonwealth spending on payments to individuals (per cent of GDP)**

	2001-02	2006-07	2011-12	2021-22	2031-32	2041-42
Age and service pension	2.93	2.83	2.90	3.64	4.28	4.59
Disability support pension	0.91	0.72	0.79	0.84	0.85	0.86
Parenting payment (single)	0.59	0.60	0.61	0.61	0.61	0.60
Unemployment allowances	0.85	0.78	0.71	0.59	0.49	0.41
Family tax benefit	1.57	1.34	1.22	1.08	1.01	0.93
<b>Total</b>	<b>6.85</b>	<b>6.26</b>	<b>6.23</b>	<b>6.76</b>	<b>7.24</b>	<b>7.38</b>

Source: Commonwealth Treasury, *Intergenerational Report 2002-03*, p. 44.

6.10 The Committee reiterates its observation from its earlier report into *Superannuation and standards of living in retirement* that the ageing of the population, together with the declining participation of mature age workers in the labour force, will place some strain on the superannuation system.

6.11 However, the Committee notes that despite some strain on the superannuation system, there is no funding crisis in the pension system, as is presently the case in

2 Committee Hansard, 15 May 2003, p. 272.

3 Commonwealth Treasury, *Intergenerational Report 2002-03*, p. 44.

some European countries, most of which guarantee a non means-tested pension at a fixed proportion of a retiree's salary, in some cases as high as 70 per cent. In Australia, the basic pension is comparatively very low, and income and means-tested, making it considerably less expensive to maintain than its European counterparts.

## **Economic growth and productivity**

6.12 The Committee also notes evidence to the inquiry that more progressive transition from work to retirement in Australia will contribute to maintaining and increasing economic growth and productivity in Australia, increasing gross domestic product and therefore the capacity of government to fund retirement incomes and services in the future.<sup>4</sup>

6.13 Through the early withdrawal of mature age workers from the labour force, Australia is losing individuals from the workforce with considerable skills and knowledge in all industries and occupations, with associated implications for Australia's productivity and income and social security systems.<sup>5</sup> With lower productivity, the gap between GDP growth and CPI growth narrow, as a consequence of which, CPI safety net payments become a higher proportion of GDP. This point was made by a number of parties to the inquiry. For example:

- the WA Department of Education and Training argued that economic growth is driven by both rising productivity and growth in the workforce.<sup>6</sup>
- The NSW Committee on Ageing noted that low participation by mature age workers in the labour force entails lost skills and experience for industry, and less tax revenue and increased social security payments for government.<sup>7</sup>

6.14 The Committee also notes evidence from DEWR that in the Prime Minister's speech of November 2002, *Strategic Leadership for Australia – Policy Directions in a Complex World*, the Prime Minister highlighted the need to ensure:

that the skills and experience of older Australians are fully utilised and that the social safety net is focused on those in need, yet does not deter participation and self-reliance.<sup>8</sup>

## **A self-correcting problem?**

6.15 During the inquiry, the Committee was presented with evidence that the current under-employment of mature age workers, and the pressure on the retirement incomes system, may be addressed in the future simply by labour force pressure for

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4 *Committee Hansard*, 15 May 2003, p. 270.

5 See *Committee Hansard*, 5 May 2003, p. 93.

6 *Submission 37*, WA Department of Education and Training, p. 1.

7 *Submission 2*, NSW Committee on Ageing, Attachment A.

8 *Submission 29*, DEWR, p. 22

mature age workers to remain in the workforce as the absolute numbers of workers declines. This pressure is likely to be determined by a number of factors, including fertility rates, immigration patterns and Australia's ongoing population policy, the state of the economy, and ongoing trends in labour productivity.<sup>9</sup>

6.16 This position was expressed most clearly by Dr Kates from ACCI during the hearing on 15 May 2003. Dr Kates argued that in the future, as the number of people of what is currently considered to be working age declines, businesses will seek out people with talents and skills in their 60s and 70s to fill positions. Dr Kates continued:

What will, in fact, happen is that businesses will recruit mature age workers and the demographic of certain jobs will change so that those you think would be taken on by young persons will often be switched to older persons. The more physical kinds of work may be taken up by younger people and the less physical, office type work will be taken up by people who have traditionally worked in offices but will continue to work there longer. The demand side by employers will make a huge difference as to how this demographic problem is handled.<sup>10</sup>

6.17 Indeed, the Committee notes anecdotal evidence from Dr Parkinson of ARPA(SA) that mature age workers are already taking on jobs previously once taken by younger workers:

I can give an example of what is happening. I notice that in the last six months, instead of my free suburban newspaper being delivered by a boy on a bike, it is now delivered by a lady who is probably in her late 50s or early 60s walking around. I think it is the beginning of that change. I find that the young people of my grandchildren's generation who are now 14 or 15 are now finding different sorts of things. I have a 14-year-old grandson who works after school in a computer repair and software provider's business. His friends tend to be doing things a bit different from going to McDonald's and so on.<sup>11</sup>

## **The need for flexible employment and phased retirement**

6.18 Given the decline in labour force participation of mature age workers in Australia, the Committee notes that in its written submission, the Council on the Ageing (COTA) National Seniors Partnership cited a recent report by BIS Shrapnel released on 21 January 2002 highlighting the need for a coordinated response to Australia's ageing population. The study found that ageing of the workforce will halt the growth of the workforce by the late 2020s, requiring the enhancing of the skills of

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9 See *Committee Hansard*, 5 May 2003, pp. 81-82.

10 *Committee Hansard*, 15 May 2003, p. 247.

11 *Committee Hansard*, 9 May 2003, p. 184.

mature age workers and the opening up of options for flexible employment and phased retirement.<sup>12</sup>

6.19 The Committee acknowledges that there are likely to be labour force pressures in the future which encourage mature age workers to remain in the workforce. However, the Committee also believes that the Government should look to encourage options for flexible employment and phased retirement in Australia. This is addressed in the following part of this report.

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12 *Submission 31, COTA National Seniors Partnership, p. 7.*