

**AMP CEO Craig Meller
CEDA speech, 30 September 2014
“Grey Expectations”**

Good morning.

Today I would like to outline our views at AMP around three issues.

The first is the fiscal and personal financial challenges presented by an aging population.

Where we need to lift the national debate from one about whether budget proposals are fair, to one about the financial sustainability of our country, and the critical need to encourage our citizens to save more.

The second is the need for quality financial advice that flows from the need to save more – particularly for Australians nearing retirement – and why we believe it is in the consumer’s best interest that that advice is delivered by companies like AMP.

And – finally – I would like to start a discussion on what really good financial advice looks like.

I think we’d all agree that it’s a noble ambition for a country, that its citizens should be prosperous in retirement.

And there’s no doubt prosperity is also an important aspiration for the individual citizen.

Indeed, we all hope to be the people who maintain their lifestyle once they stop work, the people whose “next phase” matches the sun-kissed images our industry likes to portray in the brochures.

And we all hope to be citizens of a wealthy, stable country: a country that provides well for its people, and where those people are happy to raise their families and grow old.

But the reality – at a national level *and* at a personal level – is a long way from this shared vision of prosperity.

The reality of retirement for millions of Australians is shifting, uncertain and increasingly worrying.

And for the nation, the picture looks equally unsettling.

But for Australia and most of its people, that picture is a long way off, and that makes it all too easy to stick our heads in the sand and continue to live for today.

Today, for every retired Australian, there are around five people working and paying taxes.

By 2050, that number will drop to just over two and a half working people for every person who's retired.

This is a demographic certainty. And it has significant ramifications for the nation's future finances.

As individuals and as a nation, we need to take decisive action to preserve and enhance the prosperity of our increasingly large numbers of retirees.

And we need to do this at a time when the number of taxpayers per retiree is declining.

Working against us as individuals are three factors.:

- One, we're working for fewer years than we should.
- Two, we're living longer than ever.
- And three, we're not saving enough for retirement.

A colleague of mine uses a great story about his family to illustrate this.

His grandfather left school at 14, worked until he was 65 and died at 67 – that's 51 years of work for 16 years of learning and leisure.

His father left school at 18, worked until he was 60 and lived to 77 – 42 years of work for 35 years of learning and leisure.

My colleague left education at 21, plans to retire when he's 55, and is statistically likely to live until he's in his early 80s. That's 34 years of work and 48 years of learning and leisure.

Now, I'm no economist, but that just does not add up.

And with a future that will see a doubling in the number of retirees per worker, the fiscal challenge ahead of us will make the current one look like child's play.

In a relative sense, Australia has made good progress, but clearly there's room, and the need, for improvement.

We need to take action now to counter what is the most predictable threat to our prosperity over the next 20 to 30 years.

Achieving the prosperity we desire requires planning and action at two levels: the national level and the personal level.

So what might prosperity look like?

For Australia, it looks like:

- a healthy pool of national savings supporting national investment,
- future generations unburdened by debt,
- and lower levels of taxation.

It's a society financially able to help those who need it, with older citizens enjoying well-funded, comfortable later years.

For those older citizens, it's a retirement of independence and pride, of contribution and participation.

For many it's financial freedom – and that means choice: choice of lifestyle, choice of care, choice about working after supposed “retirement”.

But the harsh reality is that, for many Australians, financial freedom in retirement is a pipe dream, so the draw on the public purse will only increase as we inch closer to the demographic reality.

But I am an optimist.

This is something I'm confident we can resolve, but only if we have reasoned public debate around the long-term affordability to the public purse of an aging population.

Unfortunately, this debate – which was started by the Government as they launched this year's budget – appears to have been lost in the headlines and political manoeuvring around individual elements of that budget.

In 2006, the United Kingdom Pensions Commission published the simplest summary of options available to address the growing financial burden of an aging population in that country.

It concluded there were only four options:

- first: save more,
- second: work longer,
- third: increase taxes,
- or, fourth: be poorer.

Some economies around the world have tried to stave off these hard decisions.

Several southern European countries serve as cautionary tales of what we could expect if we don't get a handle on our challenges.

By borrowing to support unsustainable welfare systems, they have only delayed the inevitability of their citizens being poorer.

It worries me that, in Australia, we are sliding down this path.

No one wants to be poorer, and no-one wants to pay more taxes, but it's inevitable if we don't make some tough calls.

So the other two options at which the UK arrived – saving more and working longer – should surely be the subject of more considered debate.

Australia may be better off than most, but despite the fact we've been required to save 9% of our salaries via superannuation for more than 20 years, 6 in 10 retired Australians still draw the full age pension and 8 in 10 still receive some pension support¹.

So we have a challenge at two levels.

First, our country needs to promote policy that incentivises people to save more, and encourages them to work longer and budget for an affordable income in retirement.

And second: we need to *help* individuals save more and make the best use of what they have.

The first part of the challenge is around good, sensible public policy.

Public policy must be grounded in what's best both for the nation and for individuals.

It must navigate the present, but ensure future prosperity.

So we need to address structural issues relating to our federal budget: a shrinking revenue base with growing expectations about what governments should fund.

I would urge all stakeholders to lift the debate to the critical issue of ensuring that this country learns once again to live within its means.

Within our sector of the economy, it is critical that public policy around super and retirement savings encourages people to save more and draw down an appropriate income in retirement.

We seem to be stuck in a seemingly endless round of discussions and review about what our public policy should be in superannuation, retirement incomes and financial advice.

Sadly, those discussions seem to be missing what's important: how we deliver the best outcomes for Australians.

We've had the Cooper Review, the Ripoll Inquiry, the Future of Financial Advice reforms.

¹ Actuaries Institute, Financial System Inquiry submission, 30 March 2014

We've had Stronger Super, the rewriting of our rules for prudential regulation in Australia.

We've had the Senate committee inquiry into ASIC. We've had 9% to 12%, now back to 9.5%.

And we are in the midst of the Financial System Inquiry, a Parliamentary Joint Committee inquiry into financial advice and another Senate inquiry into financial advice.

I think that's all of them – but let me know if I missed one!

If I add up the cost of this change to AMP alone – and, believe me, I have – it's hundreds of millions of dollars.

And that is a cost ultimately borne by the consumer.

Yet despite this, it seems there's a strong desire in some quarters to re-regulate – even before the effectiveness of the last round of re-regulation can be assessed.

At AMP, we strongly believe the regulatory changes introduced in the last three years across prudential regulation, across consumer protection regulation and across superannuation regulation will work.

But they need time to be implemented and time for their effectiveness to be assessed.

We are strong supporters of this Government's approach to letting these changes bed down before embarking on any further disruption to the financial services sector.

In Australia, a successful and prosperous nation, we can be our own harshest critics.

But an objective view would say we have a world-class retirement savings system.

The superannuation guarantee was introduced in 1992 with the intention of setting more Australians up to fund their own retirements.

It was – and still is – the “second pillar” between the Age Pension and voluntary savings for retirement.

The superannuation guarantee has not only eased the burden on the public purse, but also delivered a significant investment pool that has helped fund our country's growth.

And against global benchmarks, it's delivering superior outcomes for Australians.

And on top of that, the Stronger Super reforms will ensure we continue to deliver those outcomes even more cost effectively.

But we also need to encourage Australians to save more for their retirement.

While we have many extraordinarily clever actuaries working at AMP, none can create a product that makes up for a person not saving enough.

And the simple reality is that saving just 9.5% of your earnings is not enough.

Another advantage of our system is that it gives people choice – and that's critically important.

The idea that an 18-year-old with \$1000 in super should have the same solution as a 65-year-old with \$1m is clearly flawed.

But, with choice comes the need for a degree of complexity – which creates the need for financial advice.

The provision of quality financial advice is a hot topic right now. And yet very few people I speak to understand the true nature of financial advice and where its real value lies.

Too many usually self-interested parties like to dumb down the definition of financial advice to just product selection.

This is usually a ruse to justify a particular entrenched position – and is a million miles from where the true value of advice lies.

High quality advice starts with discussing with a client their life goals – and for those nearing retirement – what they want to do when they stop work.

Many of our advisers tell us, this can quickly become a process of marriage guidance as couples assess the prospect of life together after work.

It then involves an assessment of the financial viability of achieving the clients' life goals and a process of rebudgeting and planning to achieve a suitable post-retirement income without having a negative impact on short-term spending.

It may then progress to the clients' attitudes to risk in investing and possible risk mitigation strategies. Then it's about asset allocation and product category selection.

And that's about 90% of the process – and we haven't even arrived at product selection.

Indeed, in an increasingly commoditised product world, product selection is the least important component of high quality financial advice.

And that is why AMP is so committed to a vertically integrated model.

Quite simply:

- we invest more in financial advice than any other business,
- we bring in more advisers to the industry than any other business,
- we train our advisers to higher standards,
- and then we stand behind the advice we provide.

We believe there's no greater level of consumer protection than that.

At AMP we support higher industry standards – and have indeed led the way on this, we support higher entry-level qualifications, and an ASIC-managed register of financial advisers.

But like any profession, we need to prove we can regulate ourselves effectively. And I believe we can.

Finally, I would like to comment on the appropriate policy and product settings for the post-retirement phase of superannuation.

This is where a growing proportion of retirement savings will sit in future – and it's fair to say that both the development of policy and product for this phase is in its infancy.

Retirees face three key risks associated with retirement income adequacy.

The first is longevity risk – the risk of living too long.

The second is inflation risk – the risk of inflation eroding purchasing power.

And the third is sequencing or market volatility risk – the risk that negative markets in the early years of retirement will too quickly erode retirement savings.

A simplistic approach to managing these risks would be to force all retirees to purchase an index-linked lifetime annuity.

The problem is, that this is a very costly exercise – upwards of one third of investment returns would need to be spent to cover the cost of the guarantee.

And this also would fail to take account of the retiree's capacity to source capital elsewhere (usually the family home) in the event of extreme GFC-type events.

High-quality advice can mitigate all these risks, except in extreme financial circumstances, and at a far lower cost than an actual guarantee.

So we want to see settings for retirement incomes policy designed to incentivise Australians to save enough to lift themselves out of the age-pension safety net.

We also want settings that incentivise levels of draw-down that ensure income can be delivered beyond a person's average life expectancy.

And we want to see the industry I'm part of, develop retirement solutions that enable Australians to self-insure for all but extreme tail risks, and allow people to enjoy the maximum possible retirement income under most likely scenarios. That's our focus at AMP.

So, to sum up.

It's a demographic certainty that an aging population will severely strain our country's fiscal position.

As a country, we need to act now to address this issue, because the changes we need to make to balance our budget will only get harder with time.

And let's not forget we only have four options: save more, tax more, work longer or be poorer.

We need to incentivise our citizens to save more and consider working longer. Our current regulatory settings – by and large – do this, so we need to allow them to bed down.

We need to understand – and learn to value – the critical role quality financial advice plays in not only enhancing retirement incomes but also managing the key risks retirees face when the time comes for them to live off their super. Our industry needs to continue to work to improve the professionalism of its participants to ensure the highest confidence in financial advice.

Australia has a world-class retirement savings system and is doing well – but complacency will turn today's strong position into a weak one tomorrow.

All the key stakeholders in our industry need to train their focus on ensuring we're working together to manage the consequences of our aging population.

Because we do not want option four – be poorer – to become our reality.

Thank you.

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