safeguarding the future

Delivering income stream products to retirees is an essential component of any super fund's suite of member solutions and critical to member retention, so how can funds increase product traction with their members and meet post-retirement needs?

Addressing this is an ongoing challenge, particularly when members' needs are diverse, but the priority for the sector is to develop a broad range of options that caters for risks, provides a comfortable and efficient retirement for retirees, and adapts to market changes.

At the June *ASFA Unpacks: Income Streams* event, ASFA's former CEO, Pauline Vamos appraised the Australian retirement system in light of the recently announced governance framework.

"For nearly a decade, ASFA has championed the concept of a retirement framework that is sustainable, governed by objectives, and delivers income in retirement," said Vamos.

"Post-retirement is not just any product or service – we have to get it right and that can be hard to do. If it's not right, the person may never recover."

Vamos believes it's important the regulator has powers to protect consumers and the sector as a whole.

"If there is a bad product, the regulator must have the power to get it out of the market. They must have the power to make product issuers and distributors more accountable," says Vamos.

How can funds deliver sustainable income products in retirement within a constantly evolving regulatory framework? AMY BRADDON reports.

"The industry needs to get this right for everyone and we must hold each other accountable."

"The industry must also drive the advice framework. It needs to cater for digital advice, look at aged care and health care and be multi-purpose. It needs to understand the spending habits and patterns of retirees.

"It's not just about collecting data, it is about understanding the research around how retirees behave, how to protect them and understanding that they are exposed to risks like elderly abuse. That's our fiduciary obligation."

According to Rice Warner, the retirement strategy starts well before a member retires and super funds and providers need to do more to assist members with their retirement plans. They suggest funds and providers need to segment members as those with small or high balances could have a different default.

Rice Warner's prediction for the future direction of default retirement products is that members should hold money in different buckets for pension payments (drawdowns) and long-term investing, which reduces risk by better matching assets to liabilities. It also reduces the risk of investors inappropriately switching out of growth at times of market stress.

Lifecycle and lifetime annuities are relatively poor default solutions, suggests Rice Warner, but a default retirement product could be developed but would need multiple strategies.

Economist, Nobel laureate and professor at the MIT Sloan School of Management, Robert Merton, believes the current approach to retirement saving must change. Merton believes applying a goals-based investing approach to providing retirement income is the solution.

"In order to provide income in retirement, it is important to set the right goals for investor portfolios and structure portfolios to meet those goals," said Merton.

"For retirement income, managing the volatility of that income in retirement is more important than managing the volatility of capital. A portfolio specifically designed to meet such a goal will improve performance over standard generic investing strategies.

"People are told it's all about net worth when what they need is monthly income. What people care about is the standard of living they will have in retirement and that is not defined by a pot of money. It is defined as a stream of income, particularly for working and middle class people who don't have lots of wealth."

Merton insists on redesigning defined contribution plans so they more closely resemble the old defined benefit plans that gave people surety of income in retirement.

"The problem is the defined contribution system that Australia and other developed nations have embraced in recent years frame the entire challenge around assets and returns. As we saw in the GFC, that's not a good metric. If your goal is income in retirement, investment value and asset volatility are the wrong measures," said Merton.

Merton believes the onus is on the super industry to gear the goal around retirement income, rather than lump sums, and give people meaningful information on reaching those goals.

"Funds have to give people meaningful information and meaningful choices. For example, if you are running short of your retirement income goal, there are only three things you can do – save more, work longer or take more risk. And if you take more risk, you have to be aware of the possible consequence and that is you could end up with even less," said Merton.

"Moving to an income-focused super strategy means funds are going to have to change how they engage and communicate with members. Instead of asking people technical questions, like how much debt versus equity do you want, funds should start by asking people what their income goal is and then show them how they are tracking towards it.

"Rather than trying to make people smarter about investment, we need to have a smarter conversation with them that gets to where they want to be." SF