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NEW AGE PENSIONERS – TRENDS IN WEALTH

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NEW AGE PENSIONERS-TRENDS IN WEALTH

INTRODUCTION

Australia, like other OECD countries, is experiencing an ageing of its population, driven by declining fertility and mortality rates. Since the mid-1970s, the total fertility rate of Australian women has been well below the rate needed for population replacement. Over the same period, life expectancy has increased, partly due to high standards of public health (Commonwealth of Australia, 2002).

The Australian Government's Intergenerational Report (IGR) (Commonwealth of Australia, 2002) projected that over the next 40 years, the proportion of the population aged over 65 years will almost double to around 25 per cent. The recent research report by the Australian Government Productivity Commission (2005) confirmed this projection. At the same time, growth in the population of traditional workforce age —15 to 64 — is expected to slow to almost zero (Commonwealth of Australia, 2004, p.3).

Over time, the ageing of our population will result in a greater demand for Age Pensions and health and aged care spending. The IGR projected that, without changes to previously existing trends, spending by the Australian Government would exceed the amount it raised in taxes by around 5 per cent of GDP by 2041-42. To put this into perspective, the 2003-04 Budget forecast was for a surplus of \$4.6 billion. A budget deficit of 5 per cent of GDP would mean that for 2003-04 the deficit would be around \$40 billion (Commonwealth of Australia, 2004, p.3). The Productivity Commission report (2005) forecasts that by 2044-45 in the absence of policy responses, the aggregate fiscal gap will be around 6.4 per cent of GDP, with an accumulated value over the next forty years of around \$2,200 billion (in 2002-03 terms).

Between 1980 and 2005, the total number of Age Pensioners increased from 1.3 million to 1.9 million. The increase in the Age Pension population has been mainly due to growth in the eligible population, partly offset by a decline in the proportion of the population in the eligible age group receiving a pension. These trends have been forecast to continue¹ (Commonwealth of Australia, 2002). However, the IGR also projects that the proportion of pensioners receiving a full Age Pension will decline, while the proportion with a part Age Pension will increase significantly. These projections reflect a growth in wealth for older Australians of Age Pension age and the impact of the maturing superannuation system.

Since the mid-1980s, the distribution of wealth across the Australian population has shifted markedly towards older Australians (Harding, King and Kelly, 2002). The share held by those aged 65 or over increased from 17 per cent in 1986 to 27 per cent in 1997. For those aged between 55 and 64 (those heading towards and just on the verge of Age Pension age) the estimated average net wealth per adult (by age of family head) rose from just under

¹ The number of Service Pension and War Widows Pensioners has been stable around 300,000 for some time and is expected to decline as veterans from the Second World War age (Commonwealth of Australia, 2002).

\$150,000 in 1986 to around \$210,000 in 1997 (Figures are in 1998 dollars, so they reflect real increases in wealth) (Harding, King and Kelly, 2002, pp.4-5).

In addition, the effects of Superannuation Guarantee legislation are starting to impact on the wealth of Australians at retirement. Superannuation Guarantee has been in place since 1 July 1992 and requires employers to contribute to superannuation for their employees. For the 2002-03 financial year and beyond, the Superannuation Guarantee requires employers to contribute 9 per cent of each eligible employee's earnings base to a complying superannuation fund or retirement savings account (RSA).

By 2050, with a fully mature Superannuation Guarantee, it is expected that no more than 75 per cent of people aged 65 or over will receive Age Pension (or service pension equivalent) (FaCS, 2003). It is also expected that around two-thirds of pensioners will receive a reduced pension because their income or assets exceed the free areas, compared with around one third of all Age Pensioners in 2002-2003 (FaCS, 2003). Workers with superannuation are projected to have an average potential spending replacement rate of over 66 per cent², that is, spending power in retirement that is 66 per cent of that before retirement (Commonwealth of Australia, 2004, p.11).

Of great interest to policy-makers, and to Australians as a whole, is whether the projected trend towards greater self-reliance among Age Pensioners is becoming evident.

As well as the environmental changes surrounding Australia's retirement incomes system mentioned above, there is an emerging opportunity from the maturing of two key data sources, SuperSTAR cubes (which provide point in time data on income support recipients) and the FaCS Administrative Longitudinal Data Set (LDS) (which provides longitudinal data on a sample of income support recipients), that allows us to look more closely at this question. These data sources contain information drawn from the systems (managed by Centrelink) that administer the provision of income support to Australians. The LDS now contains confidentialised, detailed information about asset holdings for Age Pensioners from 1999-2000 to the present - 5 years of longitudinal data - sufficient to allow some analysis of change over time. This paper uses the LDS 1% sample (covering 1% of the pensioner population). There is also a LDS 10% sample, which is considerably more demanding to use, but gives a larger sample size and more statistical significance.

Of equal interest to the issue of the wealth of Australians reaching Age Pension age is the complementary issue of whether (or how quickly) Age Pensioners draw on their savings in retirement.

The LDS provides a similarly valuable source of information on this issue, allowing analysis of change over time in the asset holdings of Age Pensioners.

This is an interim paper, drawing on the early stages of research into wealth trends for Senior Australians. The broader research plan is outlined under "Further Research" later in this paper.

This paper seeks to answer two main questions:

- *Are Australians reaching retirement with greater wealth than in the past? and*
- *Are Australians drawing down their wealth in retirement, and (if so) how quickly?*

² This includes retirement income from the Age Pension, compulsory superannuation and additional voluntary savings (Commonwealth of Australia, 2004, p.11).

Both of these questions are explored in detail using data drawn from the LDS, with some supporting and contextual information drawn from SuperSTAR cubes.

The relevant group for which there is detailed information held in the LDS is those senior Australians who receive Age Pension, either maximum rate or part rate.

Government has a strong need to understand the circumstances of Age Pensioners over time, as they are the group who call most heavily on Australia's income support system, and, particularly for part raters, the group where increasing wealth over time would have the greatest potential to reduce demands on the public purse.

Age Pensioners also form a high proportion of all senior Australians, with roughly 78% of all Australians of Age Pension age eligible for at least a part rate Age Pension (or service pension equivalent)³.

There is some information on the LDS, although without detail on asset holdings, for moderate-wealth self-funded seniors. These seniors are eligible for the Commonwealth Seniors Health Card (CSHC) and certain other benefits and incentives in recognition of their funding their own retirement. FaCS Seniors and Means Test Branch has a companion project examining the characteristics of this group.

There is no data on the LDS for high-wealth retirees, as they are not eligible for financial support under Australia's Age Pension means testing framework (explained in more detail below) and are therefore not included in Centrelink's data stores. However, these high-wealth self-funded retirees will only impact the public purse if, later in life, through reducing income or assets, they become eligible for the CSHC or income support. At this point, they would be captured by Centrelink's systems and included in the relevant data sets.

Other key data sources, particularly the Household Incomes and Labour Dynamics Australia (HILDA) survey Wealth module, provide point-in-time data that covers the wealth holdings for the whole Australian population, and therefore information on the highest wealth groups. Longitudinal data will become available when HILDA repeats its Wealth module in coming years.

There are significant technical issues related to methodology for this project. These are explained in Attachment A.

This leaves two major specific questions:

- *Are selected cohorts of entrants to Age Pension wealthier than earlier corresponding cohorts, and (if so) by how much? and*
- *What are the longitudinal patterns of change in asset values for a recent cohort of new part-rate Age Pensioners?*

³ Sources: Centrelink Superstar Pensions database, June 2004. Department of Veterans Affairs Pensioner summary statistics, June 2004. Australian Bureau of Statistics Populations Projections for Australia, 2002-2101, Catalogue No. 3222.0

RETIREMENT INCOMES POLICY

Australia's retirement income system provides a strong basis to generate sustainable and adequate income for all Australians in retirement. It combines a publicly funded pension, compulsory superannuation and incentives for people to provide for themselves in retirement.

Australia's system comprises three complementary pillars:

- the Age Pension – a publicly funded, means tested payment that provides a modest but adequate income (or income supplement) for people in retirement. The Age Pension is a flat rate payment, set at least 25 per cent of Male Total Average Weekly Earnings⁴. Currently almost 78 per cent of people of Age Pension age receive the full or a partial Age Pension (or service pension equivalent);
- compulsory superannuation contributions under the Superannuation Guarantee - an earnings-related scheme that provides benefits in retirement greater than Age Pension alone can provide. Superannuation Guarantee savings are supported by taxation concessions; and
- private savings, including voluntary superannuation supported by taxation concessions, private investments and other savings (including investment in the home).

For the purposes of discussion, it is proposed to characterise Australians as passing through three “stages” relating to retirement income.

First, the accumulation stage. During a person's working life they may contribute to superannuation and accumulate other savings, including, for many, the purchase of a home. This is reinforced by policies aimed at boosting workforce participation, by taxation concessions for superannuation, and by incentives to remain in the workforce after reaching Age Pension age⁵. Throughout this stage a person is generally self-funded and only calls on Government assistance in times of financial stress.

Second, the transition from the accumulation stage to the draw down stage. This may entail either a complete or phased withdrawal from the workforce and the beginning of a reliance on superannuation and other savings. Some people do not need Age Pension and begin ‘retirement’ as fully ‘self-funded retirees’, but may qualify for the Commonwealth Seniors Health Card, while others may qualify for Age Pension immediately.

⁴ The Government guarantees that the maximum single rate of base pension is at least 25 per cent of Male Total Average Weekly Earnings (MTAWE).

Whenever pensions are adjusted for increases in the CPI, and the new pension rate falls short of 25 per cent of MTAWE, then the Government tops up the pension so as to be equivalent to 25 per cent of MTAWE. The pension rate is never reduced as a result of indexation. If the single pension rate increases, the partnered pension rate also increases.

⁵ As at June 2004 some 9 per cent of people over Age Pension age (about 246,000 people) were engaged in paid employment. Of these, about 32 per cent (about 78,000 people) received a pension and about 17 per cent (about 41,000 people) had deferred claiming pension and had registered under the Pension Bonus Scheme.

Third (for some individuals), an increasing reliance on the Age Pension. This may entail a progressive transition to higher part-rate or to full-rate Age Pension as superannuation and other private savings are drawn down or as other income reduces⁶.

This paper examines the “destination” of Age Pensioners at the second stage in terms of their level of wealth, and then provides some initial analysis of the third stage.

RESEARCH AND ANALYSIS IN AUSTRALIA

Trends in Wealth

Incomes

Whiteford and Bond (2000) report that from 1982 to 1997–98 the real average income of older couples in Australia increased by 5.7 per cent, while the real average income of older single Australians increased by 6.7 per cent, compared to a real increase of 4 per cent for the population as a whole. As a result, the average incomes of older Australians increased as a proportion of the average incomes of the Australian population as a whole (Whiteford and Bond, 2000, p.23).

Over the same period, there was a significant decline in the proportion of older couples for whom government benefits were the principal source of income, and correspondingly a significant increase in the role of other private income (from property and investments) (Whiteford and Bond, 2000, p.23). For older couples, the proportion for whom government benefits were the principal source of income dropped from 74.7 per cent to 65.4 per cent; while for older singles the reduction was from 82.1 per cent to 79.7 per cent. (Whiteford and Bond, 2000, pp.26-27).

Assets

The assets test on pensions was introduced in 1985 to better target assistance to those with greater needs, and to ensure the effective operation of the income test (Whiteford and Bond, 2000, p.18). The rate of pension is calculated under both the income and assets tests, with the test that results in the lower rate being the one applied. While the majority of pensioners have payments assessed under the income test, the proportion directly assessed under the assets test increased from under 2 per cent in the late 1980s to just over 6 per cent in 1999 (Whiteford and Bond, 2000, p.18). From 1999 to 2002, the proportion of Age Pensioners assessed under the assets test remained relatively stable. In 2003 it rose to 7.5 per cent, and then to 7.6 per cent in 2004 (Centrelink Superstar Pensions Database, 1999-2004).

While acknowledging that the interaction of the social security income and assets test, and fluctuations in the rate of returns on investments, may influence under which test a person’s pension is assessed, it is interesting to note that the increase, from 1985 to 1999, in the proportion of Age Pensioners assessed under the assets test, corresponds with a shift in the

⁶ Pension data shows that as at June 2004 more older senior Australians receive an Age Pension than younger senior Australians, and that more older senior Australians qualify for the maximum rate of pension (as opposed to a part rate of pension).

distribution of wealth across the Australian population towards older Australians. The share of wealth held by Australians aged 65 or over increased from 17 per cent in 1986 to 27 per cent in 1997 (Harding, King and Kelly, 2002). Over the same period, the proportion of the Australian population aged 65 or over increased only from 10.5% to 12.1%⁷. For those Australians heading towards and just on the verge of Age Pension age (those aged between 55 and 64) the estimated average net wealth per adult (by age of family head) rose from just under \$150,000 in 1986 to around \$210,000 in 1997. These figures are in 1998 dollars, so they reflect real increases in wealth (Harding, King and Kelly, 2002, pp.4-5).

Trends in Asset Holdings and Draw Down

Table 1 below (from Whiteford and Bond, 2000), provides details of the average value of assets held by Age Pensioners at June 1998, as well as the proportion of those with assets who owned their own home. As can be seen from the table, the average value of assets held begins to decline around age 70-74 and continues to be less for each of the age categories until the 85-89 category where average asset holdings again increase (Whiteford and Bond, 2000, p.19).

Table 1 Average assets of age pensioners, June 1998

Age	Home owners (%)	Mean assets of those with positive assets (\$)	Mean assets of all pensioners (\$)	Median assets of those with positive assets (\$)
60-64	78	45,300	42,500	31,100
65-69	78	46,100	43,300	32,100
70-74	75	40,300	37,400	24,600
75-79	69	34,200	31,000	17,800
80-84	61	34,000	30,500	15,300
85-89	50	37,600	33,600	15,800
90 plus	33	44,000	38,700	18,400
Total	67	40,800	37,600	-

Source: Research and Analysis Section, Retirement Programs Branch, Department of Family and Community Services, 1999.

From: Whiteford and Bond, 2000.

Understanding trends in this area is important for retirement incomes policy. Data on household wealth made available from the Wealth Module in Wave 2 of the Household Income and Labour Dynamics Australia (HILDA) Survey (run by the Melbourne Institute and funded by the Department of Family and Community Services) provides the opportunity to examine more closely the overall financial circumstances, and particularly the asset holdings, of senior Australians.

Table 2 (below) shows the mean values of assets held and household income for senior Australian households in 2002. The HILDA data shows a similar trend to the Age Pension data shown in Table 1. The average value of assets held tends to decline around Age Pension age, with small but noticeable upturns, in some assets, in later years. (The upturn in asset

⁷ Source: Australian Bureau of Statistics Catalogue No.3201.0 Population by Age and Sex, Australian States and Territories. TABLE 9. Estimated Resident Population By Single Year Of Age, Australia(a)

wealth for older age cohorts shown in Tables 1 and 2 is most likely due to an increased prevalence of single senior Australians, through mortality, and resultant asset transfers⁸.)

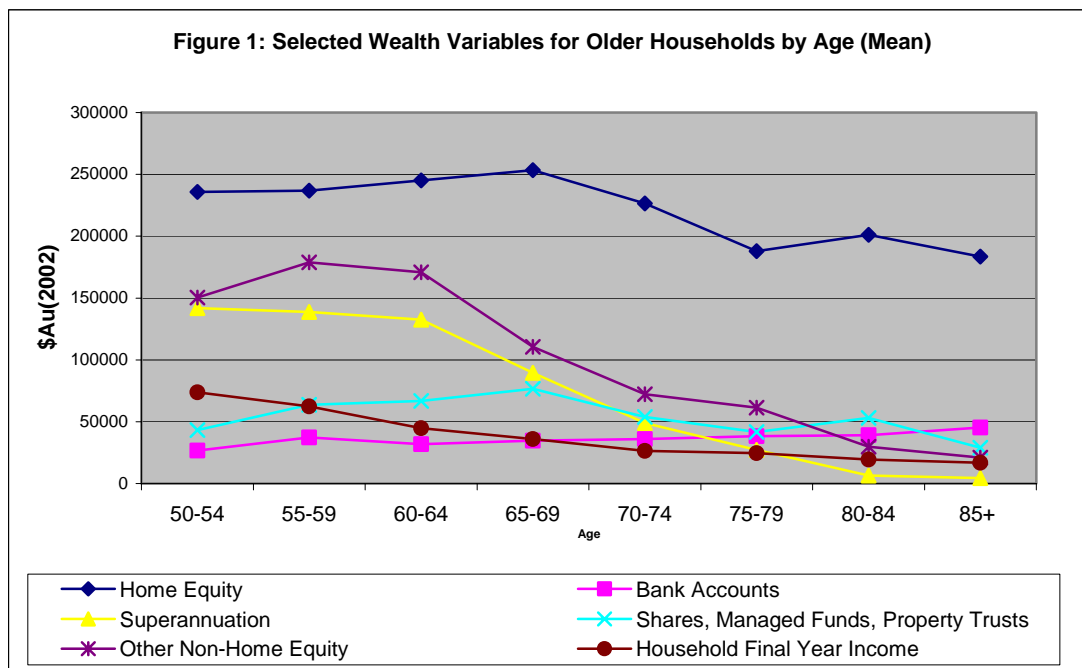
Table 2: Selected wealth variables for Households with at least one member 50 or over by Mean by Age 2002

Data source: HILDA Wave 2

Age	Home Equity	Bank Accounts	Superannuation	Shares, Managed Funds, Property Trusts	Other Non-Home Equity	Household Final Year Income
50-54	235916	26669	141896	43161	150417	73827
55-59	236809	37399	138829	63649	178910	62376
60-64	245146	31918	132536	66909	170928	44878
65-69	253346	34728	89443	76589	110568	35915
70-74	226389	35993	49015	53789	72212	26447
75-79	187805	38212	27137	41725	61228	24618
80-84	201159	39174	6532	52945	29860	19319
85+	183505	45313	4391	28986	20893	16766
TOTAL	229837	34277	96766	56383	123179	45940

Note: the HILDA data is based on 2002 values. Increases in property and other portfolio values since that time may impact on these findings.

Figure 1 below expresses the same data graphically and shows the cohort differences clearly.



These data provides some insight into what mechanisms senior Australians choose to hold their wealth and how assets may be drawn down during retirement. Any conclusion or finding of this nature is of course caveated by the fact that this is point in time data and not longitudinal; and that the more elderly senior Australians may have had less opportunity or inclination to accumulate wealth and to participate in superannuation schemes.

⁸ Superstar Pensions database (March, 2005) shows the ratio of partnered Age Pensioners to unpartnered Age Pensioners at age 65 is two to one, dropping to one to one at around age 78, and to about one in six by age 90.

INTERNATIONAL EXPERIENCE

Extensive searching has turned up little recent international longitudinal research on the question of Seniors' wealth, especially that which concentrates on the relationship between trends in assets holdings and trends in their subsequent draw down in retirement.

Ando et al (1993) studied asset 'decumulation' by the elderly, finding that the rate of decumulation was much lower than "would be implied by a life cycle model without uncertainty or bequests" (the life cycle model implies that the elderly should decumulate assets at a rate sufficient to achieve zero wealth by the time of death) (Ando et al, 1993, p.2). In other words, the pace of decumulation is too slow to be accounted for by death uncertainty alone. Ando also cites similar findings reported by Modigliani (1988), Kotlikoff (1988), Brugiavini (1987) and Ando and Kennickell (1987). While these studies varied in the reasons for the observed slowness of decumulation, they indicate that older people decumulate in a rational fashion. However, all these studies are over ten years old and do not inform current trends.

Haider et al (2000) also examined trends in 'dissaving' (decumulation) in the 1980s and early 1990s by population characteristics - marital status, age, education, health, initial wealth and others. For the 1980s, changes in wealth were fairly flat. Mean wealth grew by just under one per cent a year for the nine years of the sample period, while median wealth declined by about a quarter of a per cent a year. For a relatively young sample, aged 61 to 69, wealth stayed relatively constant. Other data showed dissaving does not begin until after the age of 70, and the age at which dissaving commences, appears to have risen over time. The 1990s data showed sample members overall enjoyed wealth increases – possibly due to a dramatic rise in stock prices for the two years of the sample period. Overall there was heterogeneity in dissaving patterns across households. The less well-off households, whether measured by wealth, income, education, or health, dissaved more rapidly than better-off households.

Important to this paper was the finding of substantial shifting of assets by older persons from housing wealth to equities, providing evidence that older investors do not passively spend their wealth but manage their portfolios actively (Haider et al, 2000). The study concluded that many of the important economic trends noted for the general population over the period had similarly affected older persons (Haider et al, 2000).

Pedersen (2004), in his study of the interplay between public and private components in the income packages of pensioners in OECD countries, used data from the Luxembourg Income Study (LIS) databank between 1980 and 1995 to examine, as one component of his research, whether it was possible to identify a general trend over time towards an increasing share of private income. Although Pedersen's research concentrated on slightly different aspects of retirement wealth to the ones in this paper, his findings do inform the question on trends towards greater self-reliance in retirement.

Whilst acknowledging that there are significant problems comparing the different pension regimes across the different countries, Pedersen (2004), in data displayed in Figure 2, shows that from 1980 to 1995 there was a general reduction in the proportion of pensioners' income from 'public transfers' (public pensions), and an increase in the proportion from private income (made up of capital income, earnings and occupational pensions [superannuation]) (Pedersen, 2004). As the countries compared have different pension systems (some with and

some without means tested benefits) it is not possible to say categorically that this shows that each generation of pensioners is successively wealthier than the last, but it is an indication that there is a general trend towards greater self-reliance. Australia (for reasons explained later), Denmark and Canada appear to be the exception.

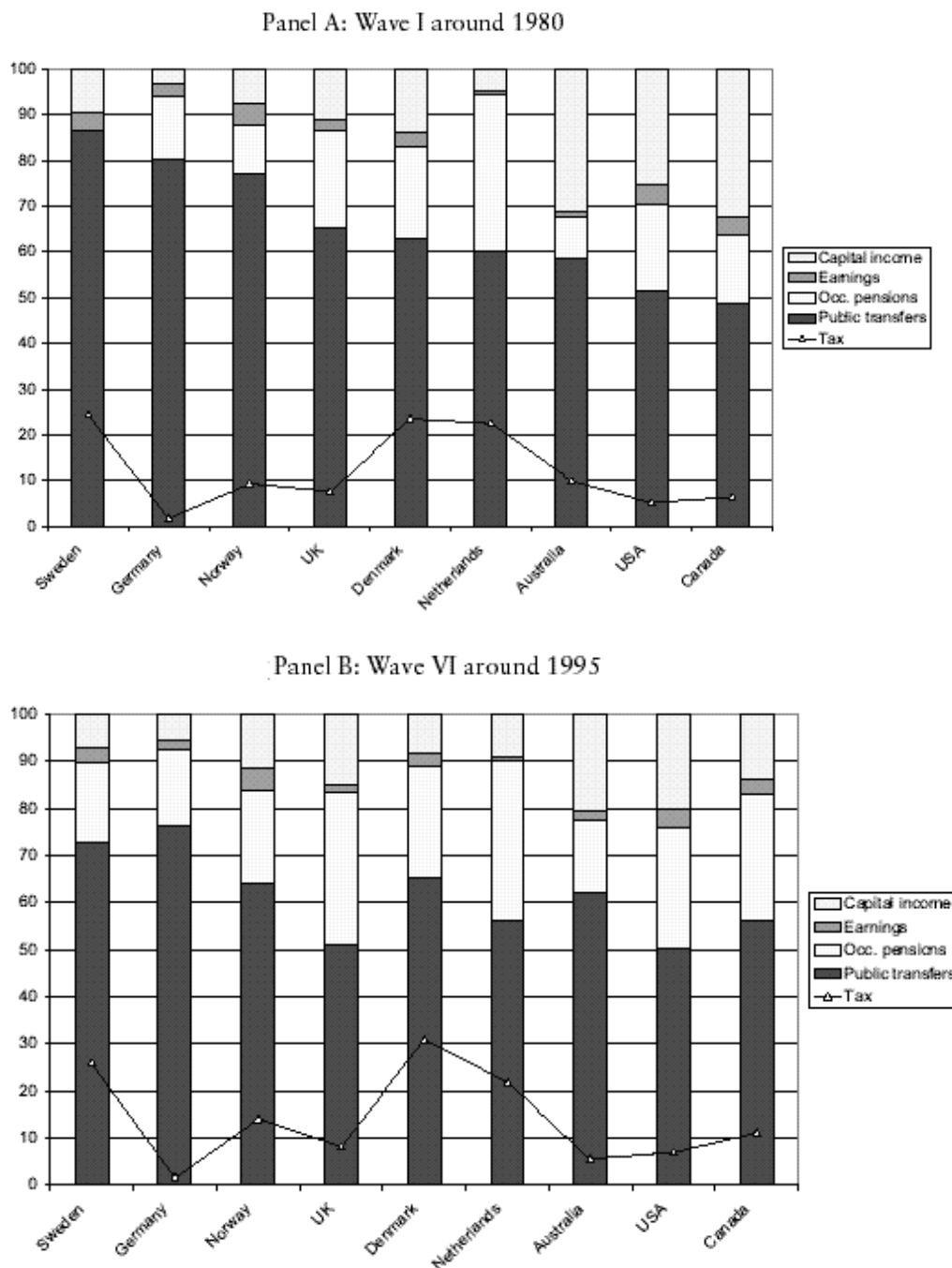


Figure 2 The share of different income components in the aggregate income package (gross income) of old age pensioners^a

From Pedersen, 2004.

Canada experienced a very different development to most – a rather consistent decline in the proportion of private income - over the 15-year period. Pedersen (2004) cites the continued maturation of the second-tier of earnings-related public pensions (The Canada and Quebec Pension Plans) as the probable explanation for this.

For Australia, there does not appear to have been a general trend in either direction. Pedersen (2004) notes that in Australia there is a preference for private sector occupational pensions to be paid as lump sums rather than annuities, and lump sum payments are not recorded in the Luxembourg Income Study (LIS). Lump sum payments will only make themselves felt indirectly in the data if the money is invested in financial assets or converted into a private annuity. Therefore, the LIS data will tend to strongly underestimate the role played by occupational pensions in the Australian retirement system.

Different findings about the make-up of Seniors' incomes and the trend towards privatisation were reported in the United States by Hungerford et al (2002), in their study: *Trends in the Economic Status of the Elderly, 1976-2000*. Despite finding that income from assets was the second most prevalent source of retirement income and made up the second largest share of aggregate income for the elderly, they also found that there was a general upturn in the level of dependence on social security by the elderly over the period 1990 to 2000.

However, Hungerford et al (2002) say that these trends, in the elderly's reliance on social security, show that these other sources of retirement income have not kept pace with social security benefits. Hungerford's study found that the proportion of the elderly receiving asset income increased from 56 percent to 68 percent between 1976 and 1984, but fell to 59 percent in 2000. A similar picture emerged with the make up of aggregate income for the elderly. Asset income grew in importance until 1984 - increasing from 18 percent to 28 percent of aggregate income - before falling back to 18 percent by 2000.

Hungerford et al (2002) cite portfolio experts as saying that, in the United States, older investors invest more heavily in safe, interest-bearing assets, such as bonds, than in assets with higher but more variable returns, such as stocks. Accordingly, it appears that the elderly are sensitive in their private savings to fluctuations in interest rates. Part of the explanation for the pattern in the receipt and importance of asset income may be the fluctuations in nominal bond yields over the period studied. Nominal interest rates and bond yields were high in the early 1980s and relatively low in the 1990s. The yield for 30-year Treasury bonds was about 12 percent in 1984 and 6 percent in 1999 and corporate bond yields followed a similar trend (Hungerford et al, 2002). The receipt and importance of asset income to the elderly increased in the early 1980s and declined over the mid-1990s, when interest rates were low.

Draw down of Assets – International Concerns

In New Zealand there is growing concern about how current and future retirees will access their accumulated wealth (St John, 2004). According to St John, in New Zealand the decumulation or draw down phase has been relatively ignored in discussions on retirement. St John says that New Zealand has few mechanisms for annuitisation of accumulated capital or for the release of home equity, but that this is beginning to be addressed – but only by the private sector and only in the form of new home equity release products (St John, 2004, p.3). The primary worry for New Zealanders, according to St John, is insufficient income and the associated danger of outliving capital.

Mitchell and Piggott (2000) say that, unlike in Australia where pension saving is mandated and pension preservation is pre-eminent, in the United States, pensions are optional, and those employees with a fund are granted substantial access to the assets. This includes the ability to borrow up to half the pension money prior to retirement, and the opportunity to cash out the fund if the job terminates. Like Australia, participants have the option to take the fund

accrual as a lump sum at retirement, and most appear to do so (Mitchell and Piggott, 2000, pp.5-6).

Stock (2004) says that banks in the United States are starting to recognise this and are starting to develop networks, marketing and products to accommodate retirees' needs for investment of lump sums and income security. In the past, the focus has been on accumulation. But now banks are realizing there are two phases of retirement - accumulation and distribution – and are expanding their product offerings to enable bank-based advisors to manage their customers' entire life cycle. Still, according to Stock, the products tend to be more for the accumulation side, and there is still a need for better fixed-return protection and investment products (Stock, 2004).

Key findings from published research

Australian and International evidence shows a very general trend in the later part of the last century of seniors having or acquiring greater wealth; both in the form of income and income producing assets; and subsequently, a trend towards greater self-reliance. However, the evidence is not conclusive and does not inform whether the trend has continued into the twenty-first century.

Australian cohort data (pensions administrative data and HILDA references) also show, as might be expected, that the older cohorts of Age Pensioners (and older Australians in general) tend to have lower assets and incomes than younger Age Pensioners. What this data does not show is the degree to which this is due to differences in the accumulation of assets prior to retirement, and to what extent it relates to draw down of assets in retirement. Recent Australian and International evidence, although abundant on the question of asset accumulation is, on this particular aspect, scant; lending itself to the conclusion that, as was found in the case of New Zealand and the United States, the relationship between pre-retirement asset accumulation and the decumulation or draw down phase of retirement has been relatively ignored.

ANALYSIS OF ADMINISTRATIVE DATA

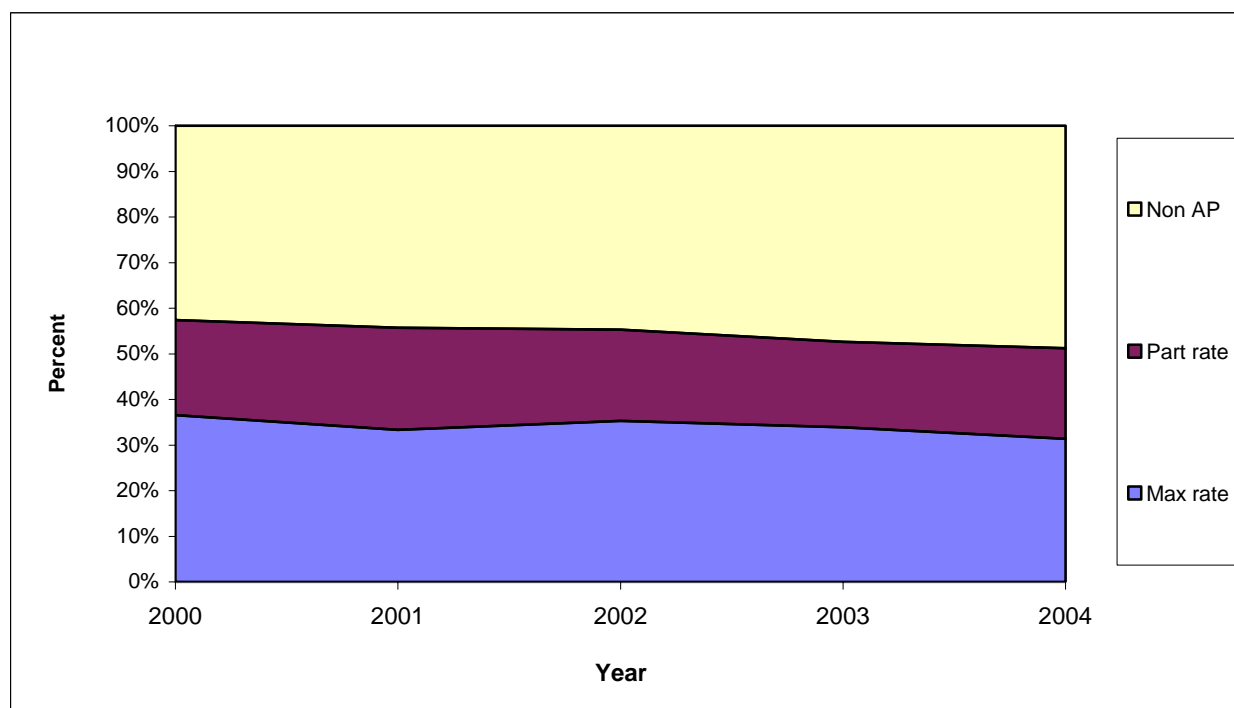
Wealth changes between cohorts

The application of the income and assets test for grants of Age Pension ensures that eligibility for and rate of Age Pension is based on an applicant's wealth (income and assets). Eligibility for and rate of Age Pension can therefore be used as a proxy for wealth.

To study wealth changes between cohorts, data has been drawn from the Superstar Pensions database for the years 1999-2000 to 2003-2004 on the number of Australians turning Age Pension age granted Age Pension, and whether that grant is at maximum rate or part rate. Figure 3 shows these data as a proportion of all Australians turning Age Pension age during the same period.

As noted at Attachment A, there are significant methodological complications to the selection and comparison of cohorts. One complicating factor is that Age Pension age for women has been progressively increasing - from 61 in 1999 to 62.5 in 2004.

Figure 3: New Age Pensioners⁹ of Age Pension age as proportion of estimated population reaching Age Pension age by rate of payment, 1999-2000 to 2003-04



Source: Centrelink, Superstar Pensions database, 1999-2004. Australian Bureau of Statistics Catalogue No.3201.0 Population by Age and Sex, Australian States and Territories. TABLE 9. Estimated Resident Population By Single Year Of Age, Australia(a)

Figure 3 indicates that a significantly smaller proportion of the total population turning Age Pension age were granted Age Pension in 2003-04 (51.2%) than in 1999-2000 (57.4%), and that this reduction is evident year on year between. The corollary of this is, over the period 1999-2000 to 2003-04, a trend toward greater financial self-reliance among Australians reaching Age Pension age, manifesting as a greater proportion not requiring Age Pension and a smaller proportion receiving maximum rate.

There are a number of factors not related to wealth or increased wealth accumulation that might have influenced this trend. A discussion on the respective influence of three factors identified as potentially significant to this trend, namely the effects of Service Pensioners, workforce participation and the indexation of Age Pension, follows.

Effects of Service Pensioners

In this interim paper, the effects of new applicants for Service Pensions have been excluded from the analysis (as the qualification rules for Service Pensions are substantially different from those for Age Pension, and data access is more complex). Service Pensioners have, in effect, been treated as self-funded for the purposes of this analysis.

⁹ 'New Age Pensioners' are defined as those who have been in receipt of Age Pension for less than one year.

However, there are comparatively few new grants of Service Pensions in any year, and the numbers of new grants of Service Pensions are declining year on year. It is expected that the inclusion of Service Pensioners in the analysis would therefore have little effect on the apparent trend to greater financial self-reliance, and that any effect would be to strengthen this trend. It is hoped that this can be analysed in future papers.

Workforce Participation

The trend may have been influenced by an increase in workforce participation by people over Age Pension age, that is, due to an increase in income (rather than assets) for New Age Pension age cohorts. A relatively small proportion of Age Pensioners are in the workforce, although this has increased slightly in recent years. At June 2004, 6.1% of male Age Pensioners and 7.4% of female Age Pensioners who turned Age Pension age during that year were in the workforce. The corresponding proportions for June 2000 were 5.1% for men and 6.2% for women (Centrelink Superstar Pensions Database, 2000-2004). Similarly, across the population as a whole, workforce participation by Australians over Age Pension age has been increasing at a significant rate. In June 2000, around 12.8% of Australians between the ages of 65 and 69 were in employment. By June 2004, this had increased to around 16.2%¹⁰ (ABS, 2005).

This small but significant increase between cohorts in the proportion of the Australian population remaining in the workforce beyond Age Pension age may result in a larger proportion continuing to be self-funded, and a smaller proportion qualifying as maximum rate Age Pensioners.

This does not necessarily negate the proposition that the trend to greater financial self-reliance is (also) due to increases in asset holdings for New Age Pension age cohorts. A proportion of this group *could* have sufficient income while in work to be self-funded, but hold few assets and therefore be more reliant on Age Pension when they eventually leave the labour force. It is counter-intuitive however, to consider this proportion to be large, as people who remain in the workforce longer could be expected to have accumulated greater assets and therefore be, on average, less rather than more reliant on the Age Pension.

In fact, as at March 2005, the average assessed assets for people who were first granted Age Pension more than one year after they reached Age Pension age were 40% greater than the average assessed assets of people first granted at Age Pension age (Centrelink Superstar Pensions Database, 2005). These later entrants are correspondingly less reliant (rather than more) on the Age Pension. As would be expected, the increasing workforce engagement of Australians beyond age 65 not only enhances their short-term wealth (income), but also contributes to and enhances future gains in accumulated wealth (assets).

Indexation of Age Pension

Eligibility for and take up of Age Pension will also be influenced by the indexation of Age Pension rates and Income and Asset test thresholds. Indexation applied to Age Pension rate is linked to the higher of the Consumer Price Index (CPI) and 25% of Male Total Average

¹⁰ Note: Analysis of this data shows extreme volatility month by month – which probably reflects the survey size. Despite this volatility, there is still a general trend towards higher workforce participation rates for senior Australians.

Weekly Earnings (MTAWE). If, as has happened with the growth of the Australian economy over the last several years, MTAWE growth exceeds CPI growth, the income and assets test thresholds for eligibility for Age Pension increase in real terms. If later cohorts had exactly the same wealth in real terms as earlier cohorts, these later cohorts would have greater eligibility for (and take up of) Age Pension. Figure 3 shows that this is clearly not the case.

As a result, subject to confirmation from further analysis, it can be concluded that the most recent cohorts of Australians are reaching Age Pension age with significantly greater real wealth than earlier cohorts.

COHORT ANALYSIS OF NEW AGE PENSIONERS

Another indicator of wealth is mean asset holdings. To determine whether Australians are reaching retirement with greater wealth, the mean assessable asset holdings of new entrants to the Age Pension system of Age Pension age have been analysed by yearly cohorts. Since they are all of Age Pension age in each cohort, such analysis facilitates grouping of people who would have faced similar opportunities and, to some extent, have similar preferences for asset accumulation. Data was drawn from the Superstar Pensions databases.

It is important to note that non-assessable assets under the social security asset testing rules are excluded, such as equity in the residential home and asset-test-exempt (ATE) income streams¹¹. With the recent increase in real estate prices and the incentives in the social security and taxation systems for these income-streams¹², these two asset types have become an important form of asset holdings for retirees.

Table 3 shows that the mean assessable asset holdings, generally, successively increased with each cohort of New Age Pensioners.

Table 3: Mean assessable asset holdings for corresponding cohorts of New Age Pensioners, 1999-2000 to 2003-04

Cohort	All	Men	Women
1999-2000	\$44,500	\$46,200	\$41,200
2000-01	\$50,400	\$51,600	\$49,400
2001-02	\$53,300	\$54,100	\$51,900
2002-03	\$52,700	\$55,300	\$50,300
2003-04	\$57,100	\$58,400	\$54,600

Source: Centrelink SuperSTAR Pension database 2000 – 2004

Note: Includes both partnered and single new Age Pensioners

¹¹ The asset-test exemption of certain “non-commutable” income streams purchased beginning 20 September 2004, changed from 100 per cent to 50 per cent. Since the sample only includes entrants to the Age Pension system from 1999-2000 to 2003-04, none of their holdings of such income streams would have been affected by this change. As a result, all of their holdings of such income streams would not have been captured.

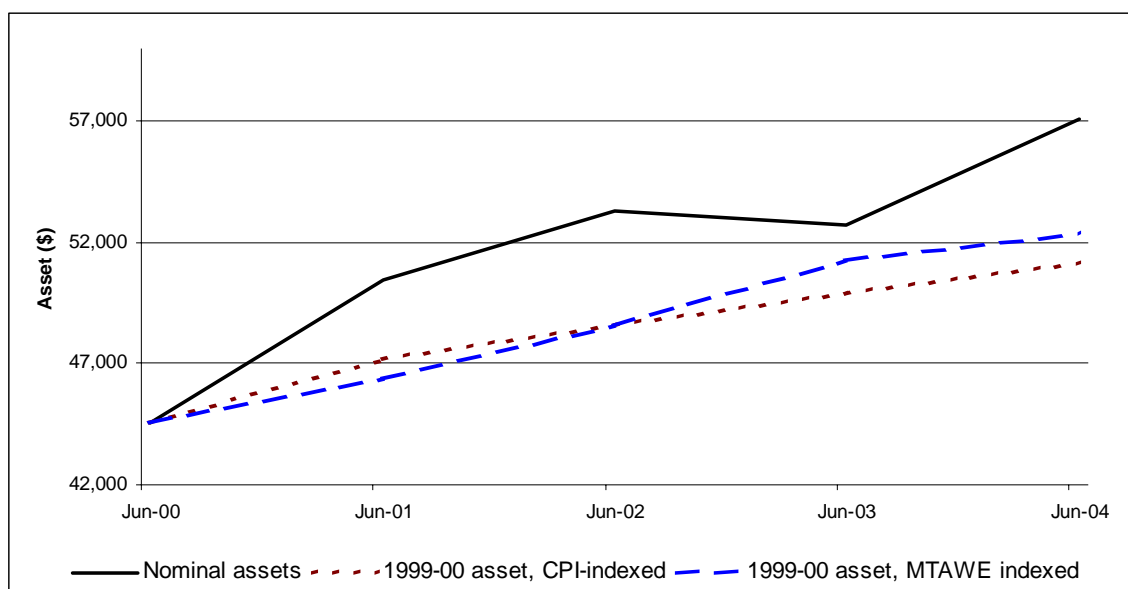
¹² In addition to the asset-test exemption, a generous income testing under the social security system also apply to these income streams where a portion of the capital used to purchase the income stream is deducted from the assessable income. Tax concessions include a 15 per cent tax rebate on the taxable portion of the pension and access to the higher reasonable benefit limit (RBL) where at least 50 per cent of a person’s superannuation is taken as a complying income stream.

It should be noted that it is the relativities of the wealth reported that is of interest. The actual reported values of asset holdings are somewhat artificial, as the cohorts exclude people who are not granted Age Pension in the year they turn Age Pension age. These ‘later entrants’ might be expected to be significantly wealthier than people who apply for the Age Pension as soon as they reach Age Pension age, as they would have been in the workforce longer (and therefore have accumulated greater wealth), and/or are only applying for the Age Pension later in life once they have drawn down some of their accumulated assets (and could therefore be expected to hold in excess of the maximum assets to qualify for a part rate of Age Pension).

To examine change in real terms, the mean asset holdings for the cohorts were then analysed further to see how the apparent increase in assets compared to price and wage increases over the same period. The assets of each cohort were plotted against the mean assets of the 1999-2000 cohort indexed for each year to CPI and MTAW.

Figure 4 indicates that the trend appearing in the later part of the last century (seniors having or acquiring greater wealth, and therefore having greater self-reliance) has continued into the earlier part of this century. As subsequent waves of new Age Pensioners arrived at Age Pension age, they did so with greater wealth, especially in their level of accumulated assets.

Figure 4: Mean assessable asset holding for New Age Pensioners plotted against CPI and MTAW, 1999-2000 to 2003-04



Sources: Centrelink SuperSTAR Pension database 2000 – 2004, Consumer Price Index, ABS Catalogue No 6401, Average Weekly Earnings, ABS Catalogue No 6302

This data not only complements the trend exhibited in Figure 3, but provides considerable evidence to support the proposition that the trend towards greater self-reliance, at least over the 2000-2004 period, is in fact understated due to the exclusion from the data of New Age Pensioners coming onto Age Pension above Age Pension age and the other factors considered above (that is, the effects of Service Pensioners and indexation of Age Pension).

While based on a relatively short timeframe, these findings appear to be in line with the IGR projections that over the next forty years the proportion of senior Australians receiving a full Age Pension will decline, and the proportion with a part Age Pension will increase

significantly - projections which reflect a continued growth in wealth for older Australians of Age Pension age and the impact of the maturing Superannuation Guarantee and other features of the superannuation system that aim to encourage voluntary superannuation contributions¹³.

LONGITUDINAL ANALYSIS OF ASSET CHANGES FOR 1999-2000 NEW AGE PENSIONERS

To examine the rate of asset draw down, the asset holdings were examined from the 517 records in the LDS 1% sample for people first granted a part rate Age Pension in 1999-2000 (see Attachment A).

These individuals were then tracked over the following 4 years, and their asset holdings and circumstances compared (in real terms) to the assets they held when they were first granted Age Pension in 1999-2000.

These comparisons are summarised in Table 4.

It is important to note that these asset totals do not include equity in the pensioner's own home. The full value of a pensioner's own home is exempt from pension means testing, and so is not captured in Centrelink's systems.

Table 4: Asset level changes for 1999-2000 new part rate Age Pensioners, 2000-01 to 2003-04

Percentage of 1999-2000 cohort who have (compared to 1999-2000 assets, real terms)	2000-01	2001-02	2002-03	2003-04
Greater assets	20.0	21.2	22.1	26.0
90 – 100% of assets	56.4	40.1	8.7	5.8
80 – 90% of assets	13.4	15.3	33.3	25.6
70-80% of assets	2.0	7.6	13.4	14.6
60-70% of assets	1.4	2.4	4.8	7.0
50-60% of assets	2.2	3.1	3.7	5.3
40-50% of assets	0.8	2.0	2.4	1.9
30-40% of assets	0.8	1.0	1.7	1.7
20-30% of assets	0.3	0.7	1.4	1.4
10-20% of assets	0.5	1.0	1.5	1.9
Less than 10% of assets	0.0	0.0	0.5	0.7
Deceased	0.7	2.4	3.7	5.4
Exited (self-funded)	0.8	2.4	2.7	2.9
Other (suspended)	0.3	0.8	0.2	0.0
<i>Total</i>	<i>100%</i>	<i>100%</i>	<i>100%</i>	<i>100%</i>

Source: FaCS Administrative Longitudinal Data Set

¹³ Examples are the government co-contribution and spouse contributions tax offset schemes.

A very significant proportion of part rate Age Pensioners accumulated additional real wealth over the period examined. In the (on average) 4½ years from being granted Age Pension in 1999-2000 to June 2004, 30% of part rate Age Pensioners increased their total assets in real terms, including close to 3% who had accumulated sufficient wealth to no longer be eligible for any Age Pension.

In addition, over 30% of Age Pensioners had, over the period, retained 80 to 100% of their assets in real terms. Most of these Age Pensioners had not drawn down any of their nominal asset holdings – the inflation over the period had reduced their real asset holdings. Over this 4½-year period, the annual reduction in real asset holdings due to inflation was 3.3%. The majority of pensioners retaining the same nominal wealth leads to the median rate of annual real draw down being the same: 3.3%. This median rate of draw down is the same between different sub-groups of these pensioners: partnered and single, homeowners and non-homeowners, and the wealthiest, middle and least wealth thirds.

It is worth noting that less than one in 13 of the surviving pensioners had, over the 4½ years, drawn down more than half of their assets.

Market effects

It is plausible that patterns of wealth draw down may have been influenced by unusual market effects during the period examined.

The period from 1999 to 2004 encompassed significant growth in real terms in real estate values in many Australian centres. However, as a pensioner's own home is excluded from this analysis, only pensioners with other real estate (such as an investment property or holiday home) would show an increase in wealth through increasing real estate values.

Of the sub-group of the 1999-2000 cohort that increased their real assets between 1999-2000 and June 2004, 20.9% owned real estate assets apart from their home. Around 14.5% of the group that became less wealthy over the period owned real estate assets apart from their home.

Noting that 79% of the group that became wealthier did so without owning any other real estate apart from their home, it is likely that the impact on asset wealth of owning real estate asset is significant, but not large. Pensioners who held property indirectly (for example through property trusts and real estate components of managed investments) may have benefited from increasing real estate values. However, the available data on indirect investments is not disaggregated sufficiently to allow this to be investigated.

A significant proportion of pensioners have equities among their assets, in many cases indirectly through superannuation, managed funds and similar investment vehicles. (This indirect investment makes the proportion of pensioners with wealth in equities difficult to quantify.)

However, the All Ordinaries index at June 2004 was no higher in real terms than in June 2000, and in June 2002 and June 2003 was significantly lower than in June 2000 (in nominal and real terms). (Standard and Poors, 2005) Overseas equity markets showed similar patterns.

Even with the drop (on average) in equity values to June 2003, there was a large group (over 22% of the entire cohort) that accumulated additional wealth between 1999-2000 and 2003.

Changes in equity markets are therefore unlikely to have contributed significantly to increases in wealth.

Circumstance effects

Wealth patterns may also have been influenced by other factors other than Age Pensioners continuing to save money from their regular income.

Some pensioners may have sold their home and therefore converted assets to a form that is means tested. This effect was tracked by examining the proportion of the 1999-2000 new part-rate cohort that had changed from 'homeowner' to 'non-homeowner' status in the LDS by June 2004. (This may slightly understate this effect, as it does not capture people who have 'downsized' by selling their home and purchasing another home of lower value.)

Of the sub-group of the 1999-2000 cohort that increased their real assets between 1999-2000 and June 2004, 7% changed from homeowner to non-homeowner. Only 2% of the group that became less wealthy over the period changed from homeowner to non-homeowner.

Noting that 93% of the group that became wealthier did so without changing home ownership status, it is likely that the impact on asset wealth of pensioners selling their home is marginal.

Others may have been widowed and inherited assets from their late spouse. Using a similar methodology to the home ownership examination, this effect was tracked by examining the proportion of the 1999-2000 new part-rate cohort that had changed from 'married' to 'single' status in the LDS by June 2004. (This may slightly overstate this inheritance effect, as it might include couples that separated for reasons other than widowhood, eg. marital separation with resulting division of assets.)

Of the sub-group of the 1999-2000 cohort that increased their real assets between 1999-2000 and June 2004, 12% changed from married to single. Only 3% of the group that became less wealthy over the period changed from married to single.

Noting that 88% of the group that became wealthier did so without changing from married to single status (and therefore potentially inheriting assets), it is likely that the impact of spouse inheritances on increases in wealth is significant, but not large.

A small number of pensioners may also have inherited assets from others such as parents or siblings, but the impact of this is likely to be minimal.

In toto, it can be concluded that the only factors that are likely to have contributed to the increase in wealth of a significant proportion of part rate Age Pensioners are appreciation of real estate assets and/or savings from regular income.

With all of these factors taken into account, it still seems that the 1999-2000 cohort of part rate Age Pensioners are managing their finances well, and maintaining their wealth in a way that will be sustainable against the prospect of a long life in retirement.

Movement from Part Rate to other Circumstances

The same individuals tracked through the LDS in terms of asset draw down were then tracked in terms of movement to other categories of Pension receipt. These are summarised at Table 5.

Table 5: Pension receipt for 1999-2000 new part rate Age Pensioners, 2000-01 to 2003-04

Percentage of 1999-2000 cohort who are:	June 2000	June 2001	June 2002	June 2003	June 2004
Exited (self funded)	0.2	0.8	2.4	2.7	2.9
Part rate Age Pensioners	70.6	61.1	49.6	47.9	48.2
Max rate Age Pensioners	28.5	37.0	44.8	45.5	43.5
Deceased	0.7	0.7	2.4	3.7	5.4
Other (suspended)	0.0	0.3	0.8	0.2	0.0
<i>Total</i>	<i>100</i>	<i>100</i>	<i>100</i>	<i>100</i>	<i>100</i>

Source: FaCS Administrative Longitudinal Data Set

At first, this would seem to contradict the finding that pensioners are able to maintain a good part of their real wealth beyond Age Pension age.

However, there are a number of factors that are likely to have influenced this. Firstly, a high proportion (around two-thirds) of pensioners on part rate Age Pension are part rate through income testing (rather than asset testing). Accordingly, if these part-raters subsequently withdraw from the paid workforce after being granted the pension, their income drops and they often move from part to maximum rate. Anecdotally, it is believed that it is common for working pensioners to reduce or discontinue paid work soon after they first move onto Age Pension. This will be examined in greater depth in later research.

In addition, it is understood that many part rate Age Pensioners are first granted on close to the maximum rate, and are in a position to adjust their financial arrangements to enable them to obtain maximum rate quickly and with little disruption. Again, this will be examined in greater depth in later research.

FURTHER RESEARCH

There is further research and analysis underway in Seniors and Means Test Branch in this subject area.

As noted above, there is work underway to analyse the circumstances of moderate wealth self-funded seniors as a companion paper to this one.

Further examination of the Age Pensioner group is likely to include all or most of:

- Cohort analysis of all new grants of Age Pension, including those of greater than Age Pension age;
- Moving beyond existing largely descriptive analysis using the LDS 1% sample to draw on the LDS 10% sample and explore issues of statistical significance;

- Cross matching with HILDA data to determine how closely HILDA wealth characteristics match with the characteristics of the equivalent Age Pension population from the LDS;
- Analysis of additional factors, such as:
 - Metropolitan vs Rural/Regional;
 - Couple versus single experiences;
 - Past history of income support receipt;
 - Age at Age Pension grant date; and
 - Earned income (eg. from part time work).
- Inclusion of Service Pensioners in the analysis (in collaboration with the Department of Veterans Affairs);
- Regression analysis to determine and weight factors that correlate with asset draw down rates for the 1999-2000 group of new part rate Age Pensioners;
- Longitudinal analysis (and regression) on asset draw down of a later cohort of new part rate Age Pensioners (eg. New entrants in 2001-02);
- Comparison of draw down rates and correlating factors between cohorts;
- Stock rather than flow analysis of draw down (ie all part rate Age Pensioners as at 1999-2000, rather than only the new entrants in that year);
- Regression analysis to determine and weight factors that correlate with asset draw down rates for all part rate Age Pensioners from 1999-2000;
- Incorporation of an additional year of LDS data (due in late 2005);
- Use of 10% LDS sample dataset (analysis in this paper has used the 1% sample); and
- Modelling of asset draw down for part rate Age Pensioners to determine the rate of “graduation” from part rate to full rate Age Pension
- Future projection of likely Age Pension(er) experiences.

CONCLUSIONS

The paper sought to answer the questions:

- *Are Australians reaching retirement with greater wealth than in the past?, and*
- *Are Australians drawing down their wealth in retirement, and (if so) how quickly?*

On the first question, it is clear that the June 2004 cohort of Australians turning Age Pension age were, on average, significantly wealthier in real terms than earlier corresponding cohorts. The attributes of this increased wealth have not yet been examined in depth, and will be the subject of further analysis. However, as people become more aware of the projected changes in the social and economic environment over the next forty years and adjust their working, expenditure and saving patterns, and with the maturation of the Super Guarantee over the same period, this trend might be expected to continue.

On the second question, it is evident that the 1999-2000 cohort of new part rate Age Pensioners are, on average, drawing down their wealth in retirement. However, this draw down is apparently at a fairly slow pace. If the patterns shown persist, this would allow these pensioners to maintain significant assets through many years of retirement.

This may indicate that part-rate Age Pensioners are managing their money effectively and are drawing on their assets in a way that has regard to their expectations of a long life. This is in line with International findings reported in the concluding decades of the last century.

In addition to the findings on the rate of draw down, there is also a substantial proportion of this group who over the period examined have actually increased their real wealth. While there are a variety of factors that may have influenced this, it appears most likely to have been driven by pensioners continuing to manage their money carefully into retirement.

What these findings also address is the question around the relationship between pre-retirement wealth accumulation and post-retirement wealth draw down. Point in time age cohort data shows that the value of assets held by senior Australians tends to decline after Age Pension age; with the exception being money held in bank accounts. This suggests that retirees draw down their assets to fund their retirement at a significant rate. The LDS data suggests that this is not the case.

What the LDS data indicate is that Australia's retirement income system provides a strong basis to not only allow senior Australians to accumulate wealth leading up to their retirement but to continue to generate sustainable and adequate income throughout their retirement. Intuitively, the conclusion from the LDS findings is that the point in time age cohort data indicates that older cohorts of senior Australians have lower levels of wealth, either in the form of income or assets, because during their working lives they had less opportunity or inclination to accumulate wealth and/or had less opportunity to participate in superannuation schemes.

Methodology Notes

Cohort Analysis

New Age Pensioners and the Age Pension Age Population

As shown at Figure 3, there is change from year to year in the respective proportions of Australians who reach Age Pension age and either:

1. are granted a maximum rate Age Pension;
2. are granted a part rate Age Pension; or
3. are not granted an Age Pension (either self-funded or granted a service pension).

Not all new recipients of Age Pension apply for the pension as soon as they reach Age Pension age. Some continue to work beyond Age Pension age, and will only become eligible as they withdraw from the paid workforce. Others have sufficient assets to fully fund their retirement at Age Pension age, but qualify for some pension later as they draw down their assets.

As a result, it would be inaccurate for the purposes of this paper to use the total number of 'New Age Pensioners', that is, all those who are granted Age Pension in a given year, to represent people first coming onto Age Pension. Instead, this paper only uses 'New Age Pensioners' who have just turned Age Pension age (that is, have not come onto Age Pension more than one year after they were age eligible).

Similarly with the Age Pension age Australian population, this paper uses only those who have just reached Age Pension age in any particular year.

A complicating factor surrounds the accounting for the number of women who are 'New Age Pensioners' who have just turned Age Pension age - the eligibility age for Age Pension for women is being progressively increased to bring it into line with the eligibility age for men. By 2014, this will be complete with eligibility age set to 65 for both men and women.

The eligibility age for Age Pension for women increases by six months every two years. In the years to June 2000, 2002 and 2004 only half the annual cohort of women turned Age Pension age (61.5, 62 and 62.5 respectively). For 2000 and 2004 this presented no further complication, as it was clear from the Administrative data how many women were granted Age Pension in the year they turned Age Pension age. However, for 2002, the total number of women aged 62 first granted Age Pension would have included a number of women that had turned Age Pension age (then 61.5) in 2001, but delayed their application for Age Pension until 2002 (because they were still working or were still too wealthy to be eligible). A correction factor (based on the proportion of women who had delayed their application for Age Pension by one year in previous years) was applied to the numbers of women counted as turning Age Pension age and being first granted Age Pension in 2002. Similarly in 2001, some 62 year-old women counted as New Age Pensioners would have been eligible the previous year. The same correction factor has been applied.

Selection of Cohort for Comparison

New Age Pensioners

It is important to note that there is a ‘dampening’ effect on changes in wealth between cohorts that stems from the nature of the interaction between the wealth of the population and the means test thresholds for Age Pension.

If a cohort of Australians in one year is wealthier (in real terms) than a previous year, the ‘sample’ we have information on (i.e. those people whose wealth is low enough to allow them to qualify for at least a part rate of Age Pension) would exclude some of the people who corresponded to the wealthiest people in an earlier cohort.

As an example, if we assume that in a given year we had a population where 3% of people turning Age Pension age had wealth of 95% to 100% of the maximum wealth that allowed them a part rate Age Pension. We might assume that this 3% group is (for example) the 50th to the 53rd percentile of total wealth in the Australian population turning Age Pension age. This 3% of people would (if they applied for the Age Pension they would be eligible for) be captured in the Centrelink systems and used for the cohort comparison. Simplistically, the averages would use the least wealthy 53% of the total Australian population.

If, in a subsequent year, every person in the total population were 5% wealthier in real terms, the 50th to 53rd percentiles of total wealth would then have wealth of 100% to 105% of the wealth for a part rate pension. They would no longer be eligible for any pension, and would drop out of our cohort for comparison. The averages would then be based on only the least wealthy 50% of the population, and therefore show a lower average value than if 53% of the population (as in the prior year) was used. Thus, increases in wealth year to year are ‘dampened’ to some extent.

This would also apply ‘in reverse’, effectively dampening the effect of later cohorts being less wealthy than earlier ones by allowing more of the later and poorer cohorts eligibility for pension. (Note that this ‘dampening’ does not apply in reverse in any of the years investigated in this paper: every year showed wealth increasing over the previous year).

It is therefore believed that the increase in real wealth between cohorts turning Age Pension age, although still quite significant, may be slightly understated.

Impact of People choosing not to apply

There is also a likely effect from some seniors Australians, while they would be eligible for at least some Age Pension, deciding that they do not wish to apply. It is assumed that this effect is minor and constant over the years. As relativities between years (as distinct from total values) are the factor being analysed, this effect would not distort the findings.

Selection of new entrants from the FaCS LDS 1%

The data for the LDS is extracted as fortnightly snapshots from the Centrelink’s administrative databases – a rich collection of raw data on customer’s characteristics and benefit details. FaCS engaged the Australian Bureau of Statistics (ABS) to develop a method

to derive a 1% sample from the administrative databases. The records in the LDS 1% go back to January 1995.

For this study, the records were taken for entrants to the Age Pension system between 1999-2000 to 2003-04, since records on asset holdings of customers were not available prior to June 1999. Entrants to the Age Pension were those who, for a particular year, only had been on age pension payment for a fortnight or less. “Entry” denotes the first time they came onto the Age Pension system. Hence those who came back to the Age Pension system following a break in their stay in the system (e.g. failing to qualify the means test for a period) were not counted again as entrants.

The age pension entitlements of these entrants were used to group them into recipients of either reduced rate pension or full rate pension. To distinguish members of illness separated couples who were on unpartnered rate of pension (hence their pension could exceed the maximum rate for partnered pensioners) from other members of couples, the amount of pharmaceutical allowance received was used. In cases where entrants were entitled to backdated payments (sometimes resulting in entitlements greater than the maximum rate) or entrants’ claims had not been processed yet (resulting in age pension entitlements equal to zero), further data processing was employed. Following entry, the rate to which their subsequent entitlements stabilized was used to group them to either part-rate or full-rate pensioners.

The 1999-2000 sample for the longitudinal analysis

From 1996-97 to 2003-04, there were 9,619 observations (of new entrants) extracted from the LDS 1%, resulting in an average of 1200 observations per year. Of these, there were 5,505 observations for the 1999-2000 to 2003-04 period. There were 955 observations for the year 1999-2000 of which 589 were on part-rate. This became the final sample used in the longitudinal analysis.

The time-invariant characteristics of the 1999-2000 cohort were obtained (e.g. date of birth, sex, country of birth and partner’s country of birth) and their changing circumstances tracked down – obtaining any changes in their financial assets, marital status and home ownership. To capture these changes, key dates were flagged: their dates of entry, exit from the age pension system (not necessarily from the entire social security benefit system), death and when they received their last payments for each financial year over the period, *last benefit date*.

These dates were used in distinguishing between actual exits and suspended payments and tracking down changes in their marital status, asset levels and payment rates in between *last benefit dates*. Changes in payment rates and marital status were captured to appropriately re-categorise them as being on reduced rate or maximum rate, at the key dates. The stable rate of payment was obtained for those who were paid in arrears.

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