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HD No quick antidote for ailing super
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LP Uncertainty of defined contributions, overcomplicated taxing and underinvestment in infrastructure are superannuation problems that will last long after the election. But shifts are inevitable in the coming decade.

Superannuation is something most don't talk about or understand but with an election campaign underway, it's turned political. From one end, you have Treasury estimating the budget misses out on more than $30 billion a year in tax revenue through super tax breaks. From the other, there's Commonwealth Bank chief Ian Narev and John Piggott, a member of the Henry panel that reviewed Australia's tax system in 2009, warning the government not to use super to fill black holes now appearing in Wayne Swan's budget. Expect lots of coverage around super over the next seven months.

TD With poor returns, people are losing confidence in superannuation. They're confused. Bringing them back is the big challenge for super funds over the next five years.

We need to start thinking long-term: beyond this campaign in an environment where Australians are forced to save for their retirement; where an ageing population has an impact on the budget; and where our infrastructure is badly in need of investment. And the problem is that the models here aren't right.

According to the latest Towers Watson Global Pension Assets study, Australia's superannuation fund pool is worth $1.5 trillion, making it the fourth-largest in the world. Indeed, it's bigger than the Australian economy, growing on the back of a compound annual growth rate of more than a whopping 18 per cent over the past decade and driven by the federal government's compulsory super levy regime and the rise of the Australian dollar.

Part of the problem is that the schemes here are defined contribution, where the investment risk has been shifted to employees who have to manage their own money and convert it into a retirement income.

Once upon a time, super schemes here were defined benefit where on retirement, you would be paid a pension, often set at 60 per cent of final salary, with automatic adjustment for inflation, and with the pension continuing until you died, regardless of how the market performed. With defined benefit schemes, the risk was carried by the employer. Defined benefit schemes were products of the time: they were generally not portable, which would make them a problem in today's workforce where people change jobs several times in their working lives. Defined benefit schemes went out with flares, vintage fur coats and sequined party dresses, except in the public service – just in case you're wondering how politicians like Nicola Roxon will be retiring at the age of 46 on a pension of about $140,000 a year.

According to Towers Watson, Australia has the highest proportion of defined contribution super funds anywhere in the world at 81 per cent.

But as Alan Kohler correctly pointed out last week (Overdone schemes are toasting super, February 11), the problem with defined contribution schemes is you don't really know what you're getting at the end and to get the most out of it, you need to be able to forecast how the market will perform, and how much tax you'll be up for. If you can't find a crystal ball for all that, you need to get advice.

But even that won't be enough because the killer is tax. The government has made the system too complicated for the average punter who doesn't spend much time if any thinking about super. With the constant changes the government brings in – from July 2012, the amount of pre-tax income individuals over 50 could put into super each year was cut in half to $25,000 – or speculation it could keep tinkering with the tax concessions to generate budget savings, it's impossible to make any predictions. Constant tax changes defy any calculations.

The other big concern is getting super to invest in the infrastructure we badly need. Stuff like better ports and land transport systems to cope with imports and exports more efficiently, a national freight network and more extensive public transport in our cities.

Some regard our superannuation pool as the magic pudding that will create it – it's not. Most super funds only have about five per cent of their portfolios invested in infrastructure. The Towers Watson report made the point that Australian super funds have the strongest bias to investing in shares of the top 13 markets surveyed, with 54 per cent of assets in shares compared with 52 per cent by US pension funds, 45 per cent by British funds, 43 per cent by Canada's pension funds and only 27 per cent in The Netherlands. Canadian funds have 33 per cent invested in bonds, we have 15 per cent. Super funds are also moving steadily into the retail property sector.

Towers Watson senior investment consultant Martin Goss says Australians have invested in riskier assets because there's more upside. "If you are investing in risk, you will have bad periods,'' Goss says. "You don't expect two or three of them, but they are going to happen sometime in a 40 year life. If you don't take any risk, you'll miss all the upside as well as missing that downside and you'll probably be worse off in cash."

While some super funds have had a good run investing in infrastructure like schools and hospitals, others have come to grief in start-up infrastructure projects like the Sydney's Lane Cove Tunnel and Cross-City Tunnel, and the Clem7 Tunnel and Airport Link in Brisbane where the traffic forecasts were way out.

Super funds say infrastructure investment on average is more expensive than a straight equity investment. Apart from the massive management expense ratio or management fees, they have to bring in expertise and that's costly. The other big problem is liquidity. We're in a MySuper environment where funds are portable and where the focus is on short-term returns versus long-term vision. That seems to work against the need for funds to increase their exposure to illiquid unlisted infrastructure assets that have a 30-year time horizon.

Super funds and PPP experts have suggested the government brings in measures like 30-year infrastructure bonds – a funding model to cope with the uncertainty of traffic forecasts, with less debt and more equity (presumably held by the government) and the government becoming a buyer of last resort where it would purchase a piece of infrastructure and then sell chunks of it to funds.

All this of course goes against government policies – and this would be true of any government – to keep risk off its books. Don't hold your breath.

There are no simple solutions here to get super more focused on our infrastructure – some have said if there were, they would have been implemented a long time ago – but it's the issue that any government will need to look at if it's serious about nation building.

As for the confusion and lack of confidence, super funds are already moving in the direction of creating a model where they will tailor products for each individual member rather than sending out generic statements. That will require a completely new skill set.

While superannuation will not come up in conversations after this election, it will be fascinating to see how it changes over the next decade. The model here needs to be fine-tuned.

Watch this space.

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