

MAY 2011

**KiwiSaver still remains the #1 strategy for retirement saving – by a country mile.**

**The Budget changes retain KiwiSaver's attractive fundamentals.**

### BACKGROUND

After the Government's signalling in February that the design of KiwiSaver was up for review, followed on May 12th by the announcement of certain KiwiSaver cutbacks, the Budget will have disappointed the 'hand out brigade' yet I suspect pleased those who seek stability in their long term retirement planning.

KiwiSaver has been wildly successful in its adoption by New Zealanders – many of whom initially signed on to get the Government's Kick-start payment of \$1000 plus the annual Member Tax credit of up to \$1042.

Add to these a member's individual contributions plus employer contributions, then employed KiwiSaver members have typically been having credited to their individual KiwiSaver accounts between 5% and 6% of their gross annual earnings. While this is less than the Australian employee's 9% annual contribution rate to their superannuation, KiwiSaver members have collectively accumulated over \$8 billion in new personal retirement savings accounts in just 4 years. These are forecast to grow to \$25 billion by 2015 and \$60 billion by 2021.

Of the sums credited to individual KiwiSaver accounts, for most adult KiwiSaver members, only 35-50% has come out of each of our back-pockets. This means each such member has been getting a top-up on their own contributions of between 100% and 200% – and that's before the KiwiSaver scheme fund managers generate a return (usually positive) on those collective savings.

### WHY IS THIS A PROBLEM FOR THE GOVERNMENT?

Not only was KiwiSaver designed prior to the Global Financial Crisis and the Christchurch earthquakes, but it has also had a far bigger take-up than was anticipated prior to its 2007 launch.

KiwiSaver was forecast to gather 186,000 members in its 1st year and have 680,000 members by 2014. In fact it attracted 716,000 members in its 1st year and now has over 1.7 million members. This number is still growing by over 200,000 members per annum. That's around 3 times the take-up predicted in Treasury forecasts made in 2006.

The resultant cost to the Government via KiwiSaver subsidies and in their role as an employer was over \$1.0 billion in the 2011 financial year and, without adjustment, the Government's KiwiSaver costs can be expected to grow by over \$200 million per annum over each of the next few years.

Again, around 3 times what was originally anticipated and most likely well in excess of what the Labour Government thought it could afford.

### WHAT'S CHANGED IN THE BUDGET?

The ongoing Member Tax Credit maximum paid by the Government of up to \$1042 per member per annum has been reduced to up to \$521 per member per annum (starting 1 July 2011). This has been effected by dropping the crediting rate on individual contributions from \$1 for \$1 to 50c in the dollar.

To ensure that the overall contribution rate of employed KiwiSaver members remains around 5-6% of annual income, employees will be required to increase their contributions to a minimum 3% of their gross earnings from 1 April 2013 (currently a 2% minimum) with the employer also being required to raise their minimum contribution rate to 3% of gross earnings at that time (currently a 2% minimum) (yet to be legislated).

Unfortunately, from 1 April 2012 the benefit of the increase in employer contributions to their employee's KiwiSaver account is substantially offset by the levying of the Employer Superannuation Contribution Tax (ESCT) to a maximum of 33c in the dollar on those contributions (currently the first 2% of the employer's contribution is tax free).

## WHAT HASN'T CHANGED?

The \$1000 Kick-start remains in place.

The flexibility to contribute at the higher 4% and 8% rates remain.

The ability to withdraw funds for first home purchases, take contributions holidays, transfer between providers etc, remains intact.

## THE GRIPES DON'T MAKE SENSE

It's clear that based on KiwiSaver member take-up to date, the Government neither needs to provide the same incentives to get many of us to understand and participate in the benefits of KiwiSaver nor can it reasonably afford the much higher cost of heavily subsidising this wildly successful savings scheme.

The substantial Government subsidies from day one were designed to get a decent public take-up into KiwiSaver (done).

In the Budget the Government has taken away a bit of the savings candy – and placed more reliance back on individuals to save for themselves.

However, despite the reduction in Government credits from 1 April 2013, an employee on a \$50,000 income still gets near a 114% 'top-up' on their annual contributions before any KiwiSaver portfolio returns. This 'top-up' includes the Government still handing such a KiwiSaver member up to \$521 per annum.

If anyone could gripe it would be employers who have a lift in employee costs of 1% from 1 April 2013.

## GROWTH IN FINANCIAL LITERACY CRITICAL

A real challenge still remains to increase the limited understanding many New Zealanders appear to have with respect to the real benefits of KiwiSaver.

This is driven home when one sees the results of public surveys like the latest monthly ASB Investor Confidence survey which rated KiwiSaver below term deposits from a future return prospect (only 12% rated KiwiSaver the best).

However consider the simple maths.

Post 1 April 2013 and assuming the KiwiSaver member is employed, the 'top-up' on their own contribution in each year is:

From KiwiSaver = between 75% to 130% (before any KiwiSaver portfolio returns).

Or versus what they would have got from saving into a term deposit = 3% to 5% per annum (based on current interest rates)

This is not anywhere close! It appears the message is not getting through to many that building retirement savings via KiwiSaver beats all other mainstream methods hands down.

## LAST POINTS

This 'zero' budget may have created fuel for the sceptics – however anyone either in the fund industry or anyone who is already invested in KiwiSaver and views the Budget changes as either unnecessary or unreasonable should understand that, irrespective of the changes, for the vast bulk of KiwiSaver members, employer and Government contributions continue to make it far and away the best way to save for retirement.

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