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Wealth Transfer Report

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NO MORE PRACTICE EDUCATION

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THE WEALTH TRANSFER REPORT

Over the next 20 years, there will be $3.5 trillion (AUD) either passed on to the emerging generations or spent. This is the largest and most significant intergenerational wealth transfer Australia has ever seen, and it presents a unique opportunity or alternatively a wasted chance for the next generations to significantly shape our nation's future.

This demographic 'future-case' summary report provides an overview of the factors and trends shaping Australia economically and socially. This data has been collated through demographic analysis and economic modelling of the accumulation of wealth by older Australians, and the wealth transfers from them to the following generations.

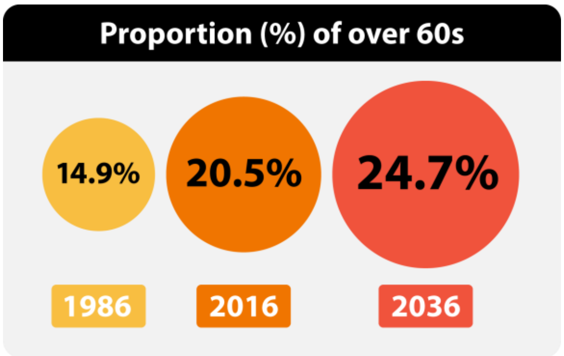
THE FUTURE RETIREMENT CHALLENGE

It is true that Australia's population is ageing, with the midpoint in our population – the median age – having increased from 30 to 37 in the span of 3 decades. This is largely due to increased longevity, with Australians living longer than ever before. So not only do we have more retirees aged 60+ who are living longer and "younger" longer (downageing), but there are also consequently more retirement years, which is increasing the total cost of retirement funding in Australia.

More retirees

With Australia's ageing population, increased life expectancy and longevity, there are more retirees in Australia than ever before.

The proportion of over 60s has increased from 15% in 1986 to 21% today, and by 2036 it will have increased to a quarter (25%)[1] of the projected population.



Living longer

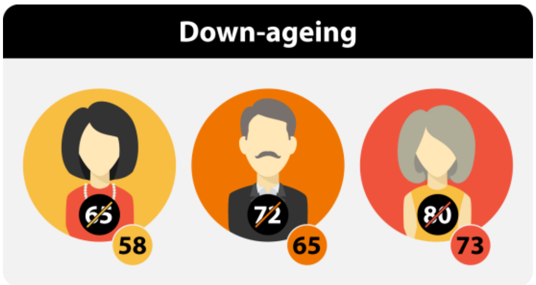
Not only are there more older people in our nation today, but Australians are living longer than ever before. In fact, those aged 65 today can expect to live 7 years longer than their parents did.[2] With Australians living longer, they are also spending longer and remaining active later in life.

[1] Australian Bureau of Statistics, Population Projections Australia, 2013

[2] Australian Bureau of Statistics, Australian Historical Population Statistics, 2014

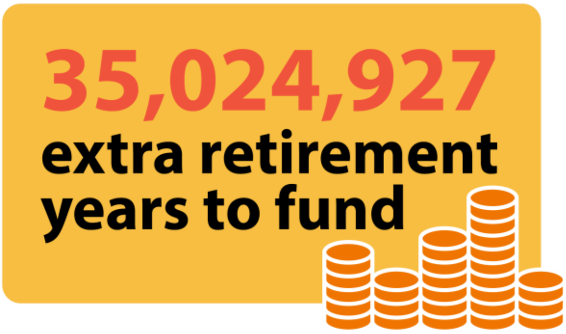
Many older Australians are in a life stage significantly younger than their age. 20th Century expectations of age can no longer be applied in the 21st Century, as traditional demographics don't match new psychographics.

From technology uptake to working longer, older Australians are not just "retired and wired" but contributing, leading and influencing later in life than has ever been seen. As such, 72 year olds today are the equivalent of 65 year olds of a generation ago based on the increased life expectancy.



More retirement years to fund

The current population of over 60s, the largest number ever seen in Australia's history, have a life expectancy 7 years longer than the previous generation of retirees. This has created a massive 35,024,927[3] extra retirement years to fund in Australia today.



Rising lifestyle costs

Not only will the Baby Boomer generation have a longer period of time in their post-working years to fund, but their lifestyle expectations are greater. The amount required per couple for a comfortable retirement is a superannuation balance of $1 million, according to the Commonwealth Bank of Australia[4].

For most, however, retirement funding comes from the Age Pension rather than superannuation alone.

The pension has more than quadrupled over the last 40 years from $204.20 per single person per fortnight 30 years ago in 1986, to $873.90 per fortnight now.[5]

During this time, however, the proportion of living costs it meets has declined. Three decades ago the Age Pension met almost all of the expected living costs for a retiree, while today on average it meets just 37% of comfortable living costs.

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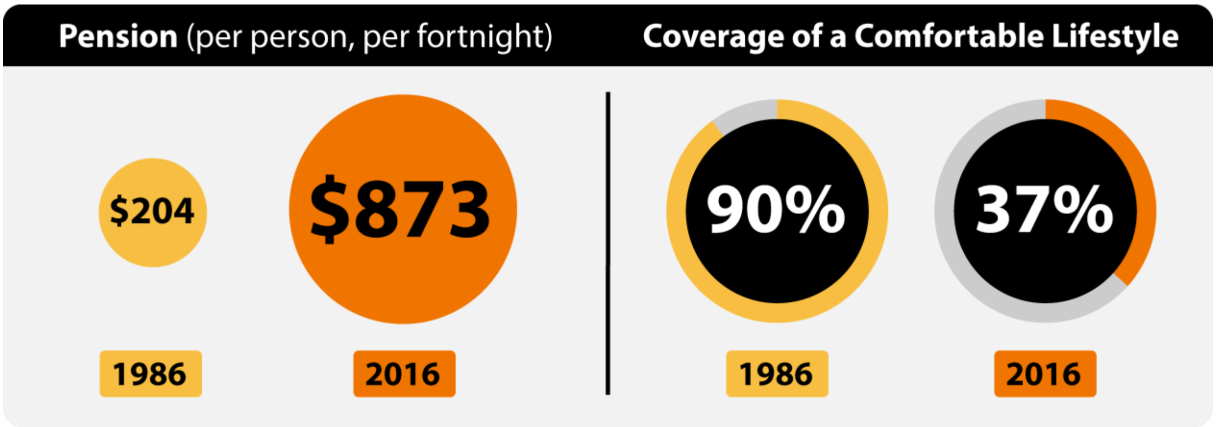
[3] An extrapolation based on the population of over 60s multiplied by the additional 7 years of life expectancy per person

[4] Commonwealth Bank Australia analysis of ASIC's MoneySmart retirement planner, 2015

[5] Australian Government, Department of Human Services, Payment rates for Age Pension, 2016



EMERGING GENERATIONAL FORECAST

Social and demographic changes, including the rising cost of living and house prices, have led to the emerging generations, the children of the Baby Boomers, delaying the traditional life markers of leaving home, starting their career and obtaining a mortgage.

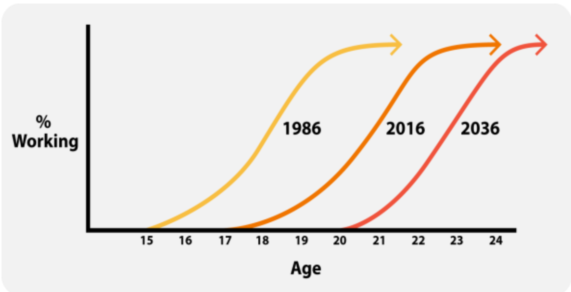
For Baby Boomers, 1 in 5 obtained a university degree compared to 1 in 4 Generation X and 1 in 3 Generation Ys, and unlike their Baby Boomer parents who largely had free tertiary education, these generations have significant study debts (HECS/HELP loans).

Not only have they commenced their earning years late in life due to more years spent in education, but they have also commenced these earning years in debt, and at a time when house prices have been at an all-time high.

Earning later

Just three decades ago, in 1986, more than half of all school students left school in year 10 to start work or vocational learning. Today, 9 in 10 students go on to complete year 12, with most going on to further tertiary study, so it is around the age of 21 that we see the biggest increase in workforce participation.

In the future, not only will nearly all students finish year 12, but half, not just a third, will go through to complete university, with many going on to post graduate studies and so the earnings years will start even later.

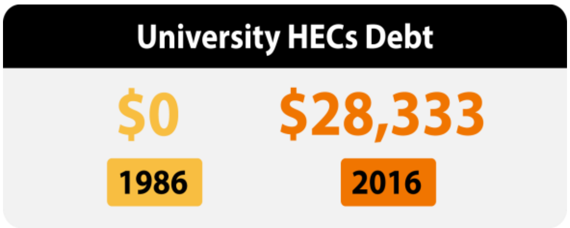


Starting earning life in debt

More than 1 in 3 (34%) registered debt agreements belong to 25-34 year olds, making Gen Y the most likely generation to be in debt.

Much of the blame is placed on easily accessible personal loans, credit card debt and a generation focused on lifestyle pursuits. Generations X and Y also have new categories of expenses that their parents didn't have such as mobile phone costs, internet expenses, tablet devices, online subscriptions and especially education debt.

While there were no university fees in 1986 today the average university debt is around $28,333 and with the growth of unregulated course costs, this amount is rapidly increasing. So these generations are beginning their earning years in debt.

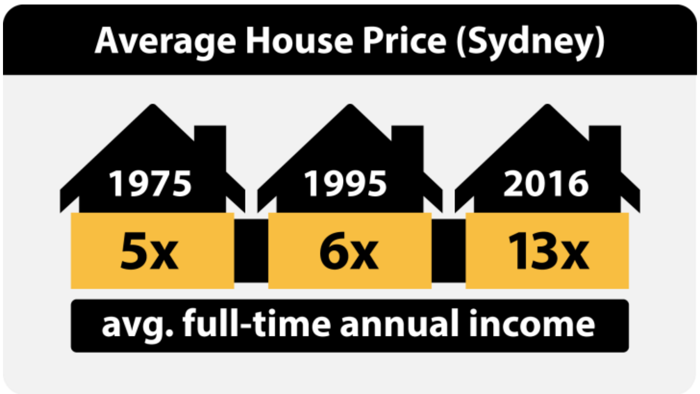


Cost of housing is greater

Not only are the costs of living higher, and the earning years starting later for our emerging generations, but the earnings have not kept pace. In the 1970s, for example, when many Baby Boomers graduated from university the average graduate starting salary was equal to the average full time adult wage, while today the average graduate starting salary of $52,500 is $26,000 less than average full time annual earnings.[6]

Furthermore, housing costs are also higher for younger people today compared to that experienced by their parents at the same age.

A generation ago the average Sydney house price was 5 times annual average earnings while today the average house price is 13x times the average annual full time earnings of $80,000.



[6] Graduate Careers Australia, ABS Cat. 6302 Average Weekly Earnings, 2016.

WEALTH ACCUMULATION – THE $3.5 TRILLION TRANSFER

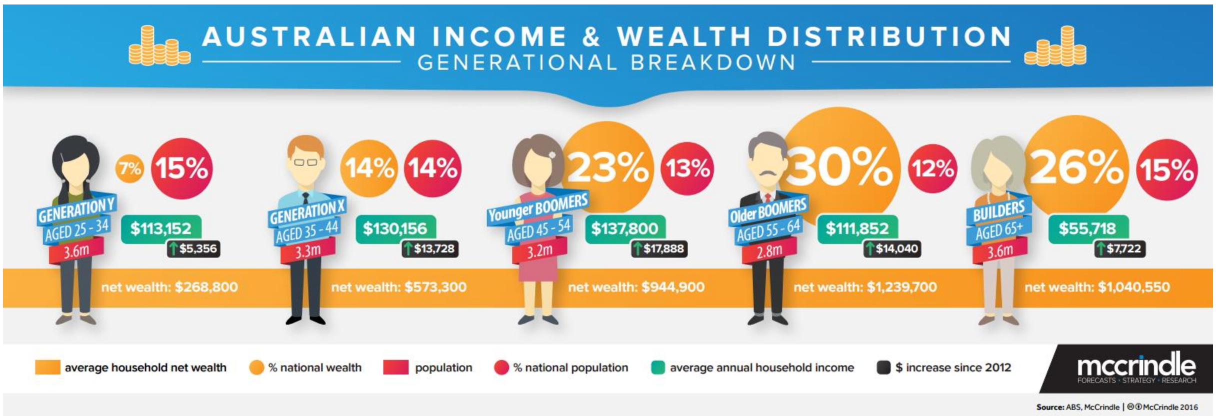
Throughout this report, financial models are presented based on available data to provide a current and future overview of wealth distribution and transfer of Australians aged over 60.

Below is an outline of the total households and average net worth of each 5-year age group. Multiplying the total households by the average household net worth provides us with the cohort net worth of each 5-year age bracket.

When we combine the current net wealth of each cohort aged 60 and over in Australia[7], the total comes to $3.445 trillion.

However, the wealth of those aged 60+ in Australia has been growing consistently over this decade by between 7% and 15% each year on average. Even if the lowest growth figure of 7% is used, this total wealth will be almost $4 trillion within 2 years, and while the over 75s are drawing down on their wealth now, the under 65s, who have the largest wealth of any Australian age group, are still wealth accumulating.

	60-64	65-69	70-74	75-79	80-84	85+
Total Households	763,313	735,441	536,363	408,572	309,758	379,903
Average Net Worth	1,239,700	1,230,200	1,230,200	850,900	850,900	850,900
Cohort Net Worth (millions)	946,279	904,754	659,834	347,654	263,573	323,259



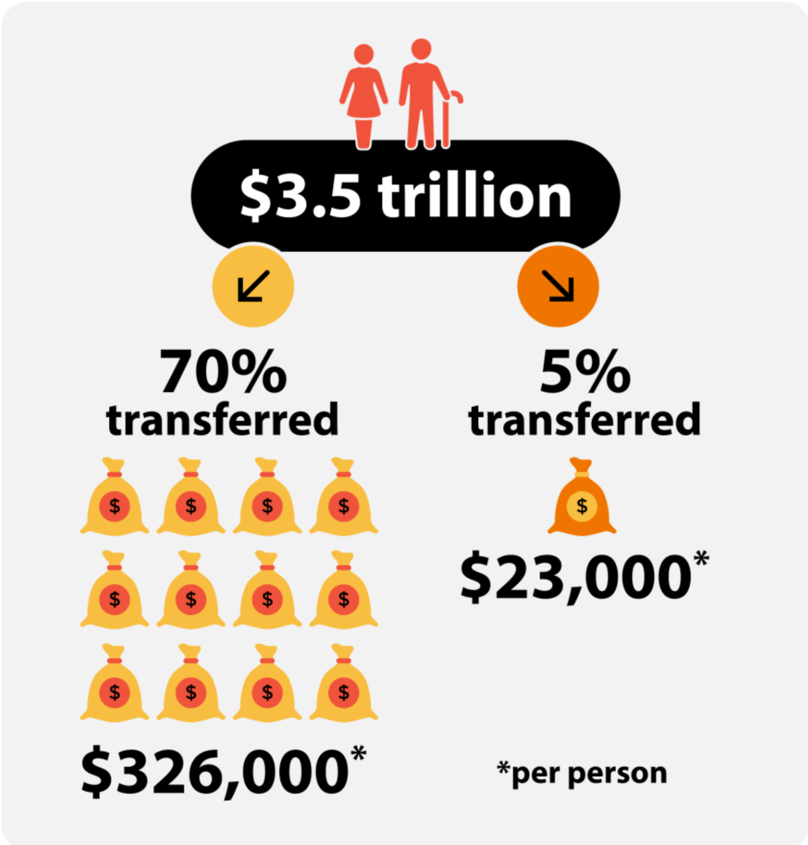
[7] Australian Bureau of Statistics, Household Income and Wealth, Australia, 2015

THE UNIQUE OPPORTUNITY

The combined net worth of those aged 60+ in Australia is around $3.5 trillion, and is growing at more than 7% per annum. Within 20 years when the youngest of this cohort will be in their 80s, 70% of this will have been spent or transferred.

The current generation of Australians 60+ have produced in total 7,522,009 children[8], and if 70% of their current total wealth (3.5 trillion) is passed on, each child would receive as much as $326,000 in wealth transferred. If just 5% is passed on, each child would receive as little as $23,000, and if all this wealth is spent then no money will be transferred. It is interesting to note that these sums are likely to be even greater as current wealth continues to grow 7% per annum until the point at which it is transferred.

Clearly this presents a unique wealth recycling opportunity for Generation's X and Y who are going to face even greater challenges than currently exist in terms of higher living costs amidst the challenge of increased ageing and reduced government capacity to fund the cost of ageing.



[8] An extrapolation based on the number of women aged 60+ and the corresponding birth rates, assuming no children have died

TWO POTENTIAL SCENARIOS FOR GENERATION X

With a potential 70% inheritance of $326,000 from their Baby Boomer parents, Generation X are faced with the option of two outcomes, either investing this inheritance and setting themselves up for the future, or spending it and not making further returns.

Scenario 1: If it is invested

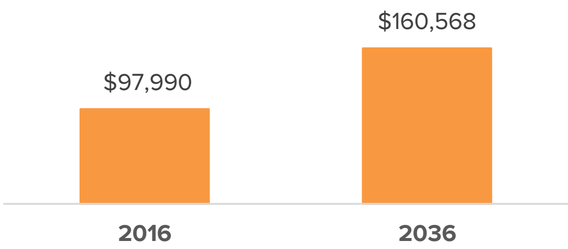
If the $326,000 inherited by a Generation X is invested in property, at a modest annual growth rate of 7.25% (which has been the annual average growth rate for residential property over the last 30 years[9]), by their retirement age Generation X's return from their inherited property investment will yield **$2,011,627** per person. This is based on the average age of a Gen X currently sitting at 44, and the average expected retirement age of 70 in two decades' time, therefore allowing for 26 years of compounding annual growth.

If Generation X invest their inheritance in Australian shares, based on the performance of Australian shares over the past 10 years at a return of 7.1% per annum,[10] by retirement age Generation X's share investment return will be **$1,939,741** per person.

Scenario 2: If it is spent

If this $326,000 inheritance is not invested but spent and used on living expenses, including housing costs, the cost of food, transport and holidays, it will be **eroded in just 2 years** from the time it is inherited. This is based on the yearly expenses of a couple with an eldest child aged 5-14 years of $97,990 in 2016[11] increasing to $160,568 in 2036 (based on an average annual inflation rate of 2.5 percent).[12]

Annual spend of couples with eldest child aged 5-14 years



[9] RBA, Long-run Trends in Housing Price Growth, 2015
[10] ASX, 2015 Long-term Investing Report, June 2015
[11] ABS Cat 4102, Australian Social Trends, 2013. The total annual spending patterns of couples with an eldest child aged 5-14 in 2009-10 of $86,871 at an average annual inflation rate of 2.0 percent between 2010 and 2016 yields total annual expenses of $97,990 in 2016.
[12] The annual inflation rate of 2.5% was recorded in Australia over the past two decades, between 1996 and 2016.

$15 TRILLION IN WEALTH RECYCLING

If the children of those aged 60+ in Australia (7.5 million individuals) take their inherited $326,000 and invest it in property, receiving a modest 7.25% in annual returns, their combined total initial inheritance of $2.45 trillion[13] could multiply six-fold, growing to a total of $15.1 trillion[14] in value by the time the average Generation X reaches retirement in 26 years' time.

This would be the truest, most successful form of wealth recycling in Australia.

THE OPPORTUNITY COST

With rising living costs, longer in retirement to fund and less government support for aged Australians in the future, Generation X will have to fund their own retirement, and will require more funds to do so than any previous generation.

Not only would the $3.5 trillion intergenerational wealth transfer be the only realistic way that most in this generation could fund their own retirement, but as shown, if this inheritance was effectively invested, it would grow to be the means of funding their own children's future as well.

To put the size of this accumulation into perspective, the total national GDP is currently $1.7 trillion so the amount of accumulated wealth to be spent, invested or passed on over the next 20 years is twice the size of the Australian economy.

The unprecedented wealth accumulation of today's retirees provides a similarly unprecedented wealth transfer opportunity, but a massive intergenerational opportunity cost if the money is spent rather than invested.

Should Generation X spend their inheritance, this would be a waste of a potential $15.1 trillion being added to the Australian economy.

[13] This assumes 70% of the current net wealth of the cohort of Australians aged 60 and over, 3.5 trillion, is passed on to the next generations.
[14] This is calculated taking the value of the yield of $326,000 invested in property (assuming a 7.25% annual growth rate over 26 years) of $2,011,627, and multiplying this value by the total number of children produced by Australians aged 60+ (7,522,009).

GRANNY FLATS OR GREATEST RETIREMENT EVER

At an individual level, the costs of this missed opportunity are also profound. If little to none of the accumulated wealth of today's retirees was passed on to their children, the investment opportunity, which will be key to funding future retirements, would be lost. Just as housing relative to earnings has increased, so retirement and aged care accommodation relative to average earnings has also increased. In a time of an ageing population, the demand for retirement housing is outstripping supply and so prices will continue to rise.

The calculated inheritance in this report will make the difference for a significant proportion of future retirees between being able to downsize into more appropriate accommodation or ageing in place with higher maintenance and opportunity costs, and for many, moving in with families. In the span of a generation we have seen the retirement ambition lurch markedly from saving to spending, and from a social value respecting the passing on of an inheritance to the championing of "spending the kids' inheritance".

The response to this once in a generation opportunity facing retirees in this Lucky Country will determine whether they retire with longevity, lifestyle and social inclusion at a level never before seen, or whether we see the return of the granny flat in great numbers- not to accommodate young people starting out in life, but as the final abode of older Australians who have simply run out of money.

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