‘Aussies do it better’: why Jeremy Hunt is casting an envious eye Down Under

The Chancellor wants Britain's pensions to be a bit more like Australia

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Jeremy Hunt picked a fight he knew he’d lose. The Chancellor was on stage at last week’s Global Investment Summit in London with Deanne Stewart, the boss of one of Australia’s biggest pension funds, when he began boasting about Britain’s sporting prowess.

Team GB’s medal haul at the Tokyo Olympics was impressive, he said, even outstripping Australia’s.

“Shall we start with cricket?” came the quip back from Stewart, before she turned to the virtues of her country’s so-called “superannuation” pension schemes.

Hunt acknowledged it was “very, very painful … for any Brit to have to point to something the Aussies do better”. But it is no secret that he wants to emulate Australia’s success in generating higher returns for pension savers.

The Chancellor admires that most people Down Under have one pension pot that follows them around when they move jobs. Underperforming funds are named and shamed, and even barred from taking on new investors.

“We’re not going to get there overnight, but we think it’s worth learning from,” says one Treasury insider.

But creating an entire pensions ecosystem is not as easy as copy and paste. So what can Britain realistically learn and emulate from Australia?

Stewart, who leads Aware Super, which has A$150bn (£80bn) under management, believes Australia’s success boils down to three factors.

“Firstly, it’s mandated for all working Australians,” she says. Second, everyone’s money is locked away. “You can’t touch it until you retire,” she adds.

The third is the fact that most people are saving in what are known as defined contribution (DC) schemes, where pension payments are based on investment returns, not the promise of a minimum income in retirement offered by so-called defined benefit (DB) schemes.

That mandate for employers in Australia means the amount they’ve had to stump up has grown from 3pc in 1992 to 12pc by 2025.

Additional employee contributions are voluntary and enjoy tax relief. By contrast, UK pension contributions demand more from the saver, who

contributes up to 5pc of the 8pc minimum.

Thirty years of growing contributions in schemes that have been consolidated and diversified have created pension funds in Australia that punch well above their weight on the global stage.

The Australian superannuation system has almost A$3.5 trillion (£1.9 trillion) in assets. By comparison, Britain's auto-enrolment is only a decade old and has around £545bn poured into defined contribution schemes in the UK.

While contributions are automatic, the system relies largely on apathy to get people saving in the first place and people can still opt out.

The UK government's intention is to eventually raise contribution rates to 12pc, split evenly between bosses and their staff. But it is understood that this will not feature in an imminent consultation on reducing the auto-enrolment age to 18 from 22.

Baroness Altmann, the former pensions minister, says higher contributions are inevitable [if people want to enjoy retirement]. "I think current contribution levels are only the very start," she says.

"Unlike in the past when British pensions were provided by employers underwriting all the risks and costs, with DC investment dependent pension funds, you can't expect big pensions from small contributions."

The Institute for Fiscal Studies has highlighted that fewer than one in 100 private sector employees actively increase their pension contribution rate in response to a 10pc pay rise.

Lady Altmann believes linking pension contributions to pay rises is no bad thing. "I'm a big fan of auto escalation," she says.

"There is nothing to stop pension providers asking their customers, after any pay rise, whether they might want to get free money from the Government

by putting some of their higher pay into their pension fund. For example, putting 1pc out of a 3pc pay rise each year would bring contributions up significantly over time. For each worker, their own money will be topped up by extra tax relief and that can increase contribution levels."

The Government's reluctance to publicly state its aim to increase auto-enrolment contributions demonstrates the difficulty in implementing such a policy when inflation is high.

Aware Super boss Deanne Stewart says governments can be tempted to view pensions as a source of funding to address economic issues Credit: CHRIS RATCLIFFE/POOL/EPA-EFE/Shutterstock

While Aware Super's Stewart believes barring savers from touching their pensions until retirement is also key to Australia's success, she recognises there is a growing risk that pots become politicised through their sheer size.

During last year's election fight, former Australian prime minister Scott Morrison promised young people they would be allowed to take up to A$50,000 out of their pension pots to get on the housing ladder if he was re-elected.

Critics' including many pension funds, said this would only pump up house prices. Stewart says pension funds must always be allowed to act in their

members’ interests.

“There’s always a temptation for governments to look to the pension system as a source of funding to address other issues in the economy,” she says.

“Funds like us can absolutely play a role in, for example, nation-building projects, but only when the risk and return profile of each investment stacks up.”

Fragmentation also remains a big problem for the UK.

Gregg McClymont, a former shadow pensions minister, notes that Nest, the biggest workplace pension scheme, is largely made up of millions of tiny pension pots from low earners, many of which have been forgotten about.

“Before auto-enrolment most private sector workers weren’t offered a workplace pension. Now not-for-profit universal schemes offer a pension to all, while for profit providers focus on more profitable larger pots.”

The average active Nest member earned around £21,000 a year in March 2022, compared with the median average of around £28,000. Meanwhile, the average Nest pension pot size last March was around £740 for women and £870 for men.

With 11 million members, these small numbers add up.

Nevertheless, McClymont says: “The challenge here is economics: there’s lots of these very small pots which are not cheap to administer”.

McClymont, who now works for IFM Investors, which invests in infrastructure on behalf of Australian pension funds, suggests that the UK should follow its lead and create a specialist vehicle representing pension funds big and small.

Australian pension funds invest around a quarter of their cash outside stocks

and bonds, compared with just 9pc in the UK, where low risk, low return bonds dominate.

“If you want to create scale collectively to drive down the costs of investment, the only way you can do that quickly is for pension funds to co-create their own vehicle,” he says.

The UK has already tried this via the Pensions Infrastructure Platform (PIP) launched by former chancellor George Osborne. For a while, it appeared to be a roaring success, with PIP working to help secure investment to finance London’s multi-billion pound super sewer.

However, an unclear mandate and a cost structure that some members believed didn’t provide value for money led to its eventual demise.

McClymont also says Australia’s move to link tax numbers to people and pensions was critical.

While the move sounds pedestrian, he says the creation of the so-called “SuperStream” or digital plumbing system that facilitated the easy movement of pension funds, was critical.

Lady Altmann says failure to make progress on this in the UK has put the country at a big disadvantage. The Association of British Insurers (ABI) notes that since 2018, the value of lost pension pots in the UK has risen by more than a third to £26.6bn, with more than 2.8 million pots now considered “lost”.

This simply does not happen in Australia where pots can be reunited with their owners easily. They are also now automatically “stapled” together following recent legislation.

Hunt may be hoping to create an army of retail investors who are engaged with their retirement funds. However, McClymont says the evidence suggests this is a red herring.

“People simply don’t engage whatever the system,” he says, highlighting a report by the Australian Institute of Superannuation Trustees (AIST), which represents the industry in Australia that noted fewer than 5pc of savers switched funds annually. “You need institutions that deliver good outcomes without expecting engagement, as in Australia” he adds.

The AIST highlighted that while pension funds are now required to tell people when they are underperforming, given that 44pc of adult Australians have a reading level of below teenage level, switching rates are still low.

In the UK, the Government’s advice website Gov.uk is written for nine year olds.

McClymont says Australia’s success is partly down to institutions being concerned about being named and shamed, and league tables which are regularly scrutinised by the industry. This alone has driven consolidation, says Stewart.

“Australia has measures in place to weed out funds that have performed poorly over the long term, and while it’s still a relatively new initiative and is still being fine-tuned, it’s already led to underperforming funds merging with better performers. In Australia, there were more than 1,500 super funds in 2004. Now there are fewer than 150.”

Lady Altmann urges policymakers to begin with the simple things.

“Pensions are free money from your employer and other taxpayers, at the same time as being able to invest in future growth companies or infrastructure or social housing,” she says.

“The positive messaging around pensions is almost never heard. All the public seems to hear is ‘you’re not saving enough’ and ‘you’re heading for a miserable retirement’ instead of ‘well done you’ve made a good start on preparing for later life’. Those kinds of positive messages of a generic nature

could start a game changing attitude.”