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Country Report for New Zealand

Prepared by

Peter Neilson, Chief Executive

The Financial Services Council of NZ Inc

Economic and Financial Background

The New Zealand economy experienced a relatively shallow recession following the 2008 global financial crisis in comparison with some other countries. Negative GDP growth for 6 quarters was followed by 4 consecutive quarters of positive growth and, after another 2 quarters of negative growth, has been positive since 2011.

Some of this growth is attributable to the amount of investment going into the rebuilding of Christchurch (our second largest city) following the major earthquakes which caused extensive damage in late 2010/early 2011.

Consistent surpluses from 2002 to 2008 have been followed by deficits in subsequent years. The centre right National-led government which assumed office in November 2008 is forecasting a return to surplus in 2014/2015.

The central Bank (Reserve Bank of New Zealand) has responsibility for maintaining inflation within a target band and implements this by setting an Official Cash Rate which is reviewed 8 times a year. In September the Bank confirmed the Official Cash Rate remains at 2.5%, unchanged since March 2011, and is expected to remain unchanged for 2013. It has, however, signalled that OCR increases are likely next year.

New Zealand has CPI inflation below 1% but this is expected to rise towards the mid-point of the 1 to 3 percent target band as growth strengthens over the coming year. House price inflation in two of the main centres is causing concern and the RBNZ has introduced restrictions on high loan-to-value residential mortgage lending, which will come into effect next month, are expected to help slow the national housing market.

Data on Funds under Management
The FSC does not collect data from members on Funds under Management. For this information we subscribe to the data published by Morningstar Research who have agreed to publication of their data in this report.

Retail Market Share Analysis year ending 31 December 2012)

Funds under Management ($M)

Portfolio	**30/03/12**	**30/06/12**	**30/09/12**	**31/12/12**
Multi sector balanced	5559.1	5420.8	6088.2	6264.6
Multi sector conservative	4658.5	4817.3	5217.7	5398.7
Cash	3862.2	4610.3	4826.8	4865.5
Fixed income	3263.7	3649.9	3852.8	4061.9
Multi sector moderate	3067.1	3267.0	3625.8	3939.6
Multi sector growth	3244.5	3223.9	3212.7	3406.0
Australasian equity	2452.4	2414.7	2693.5	2919.6
International equity	2816.6	2598.8	2544.9	2614.7
Multi sector aggressive	2159.9	2101.0	2276.7	2343.4
Property	1133.4	1156.5	1186.8	1184.5
Miscellaneous	575.9	541.8	623.4	581.6
Industry Total	**32913**	**33802**	**36149**	**37580**

Split between KiwiSaver and Non-KiwiSaver for year ending 31 December 2012

	($M) **30/03/12**	**30/06/12**	**30/09/12**	**31/12/12**
KiwiSaver	11277	11665	12912	13662
Non-KiwiSaver	21515	22137	23237	23918

Split between PIE* and non-PIE Funds under Management for year ending 31 December 2012

($M)	30/03/12	30/06/12	30/09/12	31/12/12
PIE	30219	31406	33696	35226
Non-PIE	2575	2396	2453	2354

Retail Market Share Analysis – for 2 quarters ending 30 June 2013

Funds under Management ($M)

Portfolio	**30/03/13**	**30/06/13**
Multi sector conservative	5605.3	5647.4
Multi sector balanced	6618.9	5562.1
Cash	4915.2	5193.1
Fixed income	4119.3	4192.4
Multi sector growth	3727.2	3847.6
Multi sector moderate	4224.7	3724.7
Australasian equity	3225.1	3219.4
International equity	2501.6	2598.5
Multi sector aggressive	2448.5	1607.0
Property	1266.6	1239.6
Miscellaneous	592.7	555.0
Industry Total	**39245**	**37387**

Split between KiwiSaver and Non-KiwiSaver for 2 quarters ending 30 June 2013

($M)	30/03/13	30/06/13
Non-KiwiSaver	24650	22344
KiwiSaver	14594	15042

Split between PIE and non-PIE Funds under Management for 2 quarters ending 30 June 2013

($M)	30/03/13	30/06/13
PIE	36841	35067
Non-PIE	2404	2320

*Portfolio Investment Entities ("PIEs") are managed funds that meet the eligibility requirements of the PIE tax regime, and elect in. Generally, non-PIE managed funds are taxed at 28%, regardless of an investor's marginal tax rate, whereas PIE funds attribute investment income to the investors and calculate tax on the basis of the investors' personal investment rate ("PIR"), which is capped at 28%. The top marginal personal income tax rate is 33%.

PIE and ordinary tax rates

	Ordinary Tax Rate %	PIE Tax Rate	PIE Tax Rate Advantage
Up to $14,000	10.5	10.5	0
$14,000 to $48,000	17.5	10.5	7.0
$48,001 to $70,000	30	17.5	12.5
Over $70,000	33	28	5.0

Key Trends in flows and assets under management

Since their introduction in July 2007 KiwiSaver schemes have become the favoured vehicle for retirement saving. KiwiSaver schemes are PIEs and this enables members to have their investment earnings taxed at a rate closer to their marginal tax rate, and caps the tax rate at 28%.

The trend is for non-KiwiSaver savings to also move into other PIE savings vehicles.

Product Developments

The introduction of KiwiSaver has been the outstanding product development of the past decade. The key features of KiwiSaver schemes are:

- All **new** employees are automatically enrolled by the employers – the employee has up to 8 weeks to 'opt out' if they choose.
- Existing employees may elect to join a KiwiSaver scheme.
- Members contribute a minimum of 3% of earnings but can elect a higher 4% or 8% rate. Employers contribute a minimum of 3%, but can also elect a higher rate.
- Savings are locked-in to age 65 (subject to a minimum 5 year membership). (Early withdrawal can occur on hardship, permanent emigration and death.)
- Individuals choose the fund manager they prefer from a range of approved product providers. If the individual does not make a selection then contributions are applied to a Government approved 'default provider' (currently there are default providers).
- Incentives:
    - Government provides an initial $1000 up-front 'kick-start' payment.
    - A 'tax credit' of $521pa is credited to the account of members who contribute at least $1042 per annum.
- KiwiSaver members can elect a contribution holiday after 12 months membership for a maximum period of 5 years.
- Savings can be used for first home purchase and receive a Government mortgage subsidy.
- Self-employed and non-working individuals can choose to join a KiwiSaver scheme and children can also be enrolled by a parent or guardian.

Regulatory and Self-Regulatory Developments

The level of regulation of the financial services industry has increased significantly in the past 5 years. One of the results of the global financial crisis in New Zealand was the collapse of second-tier lenders with subsequent financial losses for people (many of them retired) who had invested their savings in those companies to take advantage of slightly higher interest rates. Regulation of the financial services industry subsequently focussed on a higher level of accountability for financial service providers and their advisers.

In 2008 the Financial Service Providers (Registration and Dispute Resolution) Act brought in registration of all financial service providers. In the same year the Financial Advisers Act brought in regulation of financial advisers, controlling who may provide financial advice and what information they must disclose to their clients. This Act makes financial advisers (and the companies they act for) accountable for the advice they provide and gives the FMA the power to act in the event of non-compliance.

In 2011 the Financial Markets Authority was set up as the market conduct regulator, in place of the Securities Commission. The main objective of the FMA is to promote and facilitate the development of fair, efficient and transparent financial markets. The FMA enforces legislation in respect of financial markets participants such as issuers of securities and banks.

In 2011 the Securities Trustees and Statutory Supervisors Act set up a regime which included licensing for trustees of debt securities issued to the public, unit trusts and KiwiSaver schemes.

In September this year the Financial Markets Conduct Act was finally enacted, after a gestation of almost 7 years. This will replace financial market conduct regulation contained in a number of statutes and is intended to provide a more coherent regime that will promote confident and informed participation in financial markets. When the new Act is fully implemented (in about 2 years) it will do that by:

- ensuring that investors are provided with understandable and accurate information to guide their decision-making;
- ensuring that governance arrangements in respect of financial products available to the public are robust;
- minimising unnecessary compliance costs for those raising capital; and
- promoting innovation and effective competition

From 1 July 2013 Regulations issued under the KiwiSaver Act require public disclosure of scheme performance in the form prescribed by the Regulations and must contain prescribed information. Information is required on:

- Performance and returns
- Fees and costs
- Asset and portfolio holdings
- Key personnel, policies, valuation and pricing methodologies, and conflicts of interest.

Taxation

The main taxes are the personal and corporate income taxes and Goods and Services Tax (GST), a value-added tax.

Personal income tax rates were reduced in 2008, 2009 and 2010. In 2010 the GST rate increased to 15% and the company, superannuation scheme and PIE rate reduced to 28%.

The current rates for personal income tax are as follows:

Income up to $14,000	10.5%;
$14,001 - $48,000	17.5%;
$48,001 - $70,000	30%;
Over $70,000	33%.

All income is taxed but most capital gain is excluded. Withholding taxes apply to wages and salaries and to interest income and dividends. Fringe benefits are taxed separately.

Tax credits based on combined family income are available to families with children. A tax credit is also available to some independent earners who do not otherwise receive government support.

The tax treatment of pension funds and other savings is “TTE”, i.e. contributions are made from tax-paid income, fund earnings are taxed and withdrawals are exempt.

No other country has the same combination of comprehensive taxation of the return on debt instruments as they accrue, no superannuation tax concessions, no tax on capital gains on rental properties for most investors, and the unconstrained deductibility of the nominal value of interest against other income on debt used to purchase rental property. As a result New Zealand stands out compared to comparable economies by having one of the highest tax biases in favour of investing in real estate and against investing in financial assets.

From September 2011 a tax change was brought in to allow foreign investors in a New Zealand fund with only foreign investments to pay no New Zealand tax on their income, whether or not the fund distributes that income. This tax change was intended to make these NZ funds an attractive destination for foreign investment but there has been a limited response.

The regime has since been extended to include a foreign investment variable-rate PIE that invests its funds both in New Zealand and offshore. Notified foreign investors in this category of PIE face various tax rates, depending on the source and type of the income.

Corporate Governance – major developments
Disclosure from 1 July 2013 under the KiwiSaver (Periodic Disclosure) Regulations requires disclosure of key personnel, policies, valuation and pricing methodologies, and conflicts of interest. A table must be provided in all disclosure statements showing the directors and employees of the manager who have the most influence on the investment decisions of the fund. Quarterly disclosure statements must contain additional information, where relevant, about conflicts of interest, material changes to a fund's trade allocation and execution policies and proxy voting policies, and changes to fund valuation and pricing methodologies.

Fund Governance
The key changes in fund governance are covered in the legislation changes noted above under Regulatory Changes.

Other major issues and developments
To reduce the future fiscal cost of NZS, the previous Labour Government set up the NZ Superannuation Fund in 2001. That required the Government to set aside a sum determined annually by Treasury (initially $2 billion per annum) from surpluses, to partially pre-fund the NZ S liability from 2025. The NZ Superannuation Fund total assets as at 30 June 2013 were $22.97 billion. The current National-led Government has stopped further contributions to the Fund for the time being but has said that they will be resumed once the government accounts return to surplus.

The FSC is leading a debate on the need to increase the coverage of and contributions into KiwiSaver. There is a debate underway regarding the issue of compulsory versus voluntary membership of KiwiSaver for employees. There is consistent public support of around 60% for making KiwiSaver membership compulsory for employees. There is also a conversation, led by the FSC, on whether the contribution rate required to fund a comfortable retirement (2 times the universal age pension) could be reduced by removing the tax bias against compound return financial products and moving default funds from at least 75% conservative investments to portfolios with more growth assets.