

Introducing the

Member's Default Utility Function

VERSION 1

Creating a new paradigm in retirement planning



Background

Providing retirement outcome solutions is a hugely challenging and complex area. The superannuation industry needs to mature by developing products, solutions and strategies that meet the retirement outcome challenge.

This challenge can be met with the following framework:

COMMUNICATIONS AND ENGAGEMENT

It is critical to communicate the outcomes and benefits of the solution

PRODUCTS AND SOLUTIONS

The solution may be a blend of products, solutions and services

CLEAR OBJECTIVE

The industry lacks clarity on what it is trying to achieve for members in retirement

FOUNDATION

Sophisticated model that can project the range of retirement outcomes a member could experience

MDUF solution

Member's Default Utility Function Version 1 (MDUF v1) considers the question:

'What is a sensible set of financial preferences for a trustee to assume on behalf of a default fund member?'

We ignore behavioural biases and focus on sustainable retirement outcomes.

MDUF v1 captures preferences which are intuitive, but are not considered by other metrics. In particular, MDUF v1 recognises the following preferences:

- Higher income
- Smooth income
- Outliving savings is a poor outcome
- Residual benefit has value
- People are risk averse

The panel converted these preferences into a mathematical function, known as a utility function. This function has been named MDUF v1. Though perhaps unfamiliar to industry, utility functions have been used by academics to solve retirement outcome problems for over 50 years.

The future

MDUF v1 is a credible and powerful tool which can be used by industry, regulators and policymakers for varying purposes.

Possible applications include:

- Post retirement solution design by super funds and other product providers;
- Assessment of design by regulators and ratings groups; and
- Welfare analysis by policy groups.

The panel encourages the industry to collaborate further on addressing the retirement outcome challenge and see the sharing of this work as a step in that direction.

AIST and ASFA have both agreed to be custodians of this work. This means they support the research and are committed to making it available to the broader industry. Papers, presentations, models and FAQs will soon be made available.

To receive these resources when they are available, please contact mduf@mine.com.au

The panel

A panel of academics and industry professionals was established to research and ultimately develop MDUF v1. The panel has over 200 years of combined relevant experience.

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About the lead author

David Bell is a lead author in relation to MDUF v1 and the Chief Investment Officer of Mine. He has 20 years of experience in investments, portfolio management, retirement outcomes, and risk management. David holds a Bachelor of Mathematics (Applied Mathematics and Statistics) from the University of Newcastle and a Master of Applied Finance from Macquarie University. He is currently studying towards a PhD on investment management and is a frequent industry commentator.

Get in touch

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