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irfa dispatch

THE RETIREMENT INDUSTRY NEWSLETTER

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Spend the Income and not the capital to ensure a long-lasting retirement

Retirement can be a daunting prospect. Not only is it a time of personal adjustment but it is also a time to make financial decisions that will impact your lifestyle for the rest of your life. Retired investors commonly face the dilemma of either maintaining a certain lifestyle or adjusting it to preserve their savings.

Typically, the more income one draws and spends today, the less income one can draw in the future. When inflation is added to this quandary, it becomes important to also grow that income over time to retain one's buying power.

A drawdown rate of 6% is common in the market place but Marriott's research* shows that at that rate, almost half of retirees would have depleted their capital within 30 years. The concern for retired investors today is that markets are volatile, and returns are expected to be below average for the foreseeable future. This suggests many living annuities will come under pressure in the years ahead.

Marriott has two suggestions for retired investors:

1. Match the income drawn with the income produced
Investors should be aware of how much income their portfolio is generating and try to draw no more than the income produced – thus avoiding capital erosion. Investments that produce reliable and consistent income streams assist investors in matching income drawn with income produced. If an investor can avoid drawing more than what their investment produces they can secure their future income - this is especially important in the early stages of retirement. If investors wish to draw more income than what their investment is producing, it should be with the knowledge that they are eroding their capital

2. Choose investments which produce consistent income streams that grow over time
Investors also need to ensure they protect themselves against the impact of rising living costs over time. Investments that produce reliable income streams that also grow over time, like equities, are critical for a successful retirement. By including the right equities, those which have a reliable growing, inflation-hedged income stream, investors will be able to ensure growth in their investment income over time. The trade-off of including equities, however, is that initially an investor's portfolio will produce less income. Investors need to find the appropriate level of exposure to the different asset classes that will give them enough income and income growth over time.

Marriott's investment portfolios are managed with an income focus – to produce a certain amount of income as well as income and capital growth. This investment style is in contrast to many others where the investments are managed with a capital growth objective. The basis of a capital growth objective is that investment growth will offset the income withdrawals. This appears to work well when capital values are increasing because capital erosion is masked by the market rise. When markets decline however, the value of the investment will decrease sharply due to the twin effects of capital erosion and lower market values.

At Marriott, we suggest that investors examine their situation carefully when considering using capital to supplement their income. We recommend investors match the income drawn with the income produced by their investment until they reach a stage in their retirement years when it may become safer to drawdown on capital. While investors may find it challenging initially to restrict their annuity income to the income produced in the current economic environment, this is preferable to running out of capital. Rather be conservative now than risk having to find another source of income, such as going back to work or having to reduce one's standard of living at some point in the future.

FA News | 30 October 2018

Accessing your RA in the case of a permanent disability

It is possible to retire early from a fund if you can present medical evidence.

Normally you cannot access money invested in a retirement annuity (RA) until you turn 55. As these are retirement savings, the intention is that they should be held until you reach retirement age.

There are, however, three exceptions.

The first is if you are no longer contributing to the fund and you have less than R7 000 saved. Then you are entitled to withdraw the full amount.

The second is if you financially emigrate. The government will then allow you to withdraw everything in your RA and take the money with you. You will however be taxed at the normal rates for a withdrawal, as per the table below:

Taxable income	Rate of tax
R0 – R25 000	0%
R25 001 – R660 000	18% of taxable income above R25 000
R660 001 – R990 000	R114 300 + 27% of taxable income above R660 000
R990 001 and above	R203 400 + 36% of taxable income above R990 000

Source: Sars

Thirdly, and perhaps least well known, is that you can access your RA if you are permanently disabled. This is effectively treated as an early retirement.

That means you can take the full amount if you have less than R247 500 in the fund. Otherwise you can take up to one third as a lump sum, taxed at the below rates, and you must use the rest to purchase an annuity.

Taxable income	Rate of tax
R0 – R500 000	0%
R500 001 – R700 000	18% of taxable income above R500 000
R700 001 – R1 050 000	R36 000 + 27% of taxable income above R700 000
R1 050 001 and above	R130 500 + 36% of taxable income above R1 050 000

Source: Sars

Making an application

What is important for investors to appreciate is that the threshold for what is considered a 'permanent disability' in this case is not necessarily the same as the threshold for an insurance claim.

"As there is no risk product attached and therefore no underwriting, the definition of 'permanently disabled' is fairly loose," explains Marina Higginson, a director at GFP Financial Planning. "What is required is for the member to make an application to the board of trustees, provide medical evidence, and the board will then decide whether or not to approve it."

Boards of trustees will generally rely heavily on the medical opinion that comes with the application. Each fund may handle this slightly differently, but there will be broad similarities.

Allan Gray actuarial analyst Shaun Duddy explains that members of the Allan Gray RA would need their attending medical practitioner to provide details in three areas.

"Firstly, they must provide a reasonable level of detail on the condition or conditions that the member is suffering from," Duddy says. "Next, they must state what, in their professional view, are the chances of that member recovering from that condition. Lastly, given the combination of the condition that they face and the likelihood of recovery, do they believe that the person is, in the traditional definition, permanently disabled either physically or from a cognitive point of view."

This will then be evaluated by the board of trustees.

Medical opinion

"The ultimate decision on whether or not the member is deemed permanently disabled sits with the trustees of the relevant fund," says Duddy. "That decision is however heavily influenced by the professional opinion of the medical practitioner."

Higginson says that there may however be instances where the board cannot make a decision based on the initial submission alone.

"If the board feels that it is not able to arrive at a conclusion, they can ask for further medical evidence, particularly relating to whether this person is permanently disabled," she says. "As the board is not expected to have medical knowledge, it may also not feel competent enough to decide on the matter itself. They could then call in an expert to help them with the assessment."

What constitutes permanent disability is also not necessarily aligned with what you might insure yourself against. Insurance policies will generally differentiate between being disabled for your own occupation, your own or a similar occupation, or any occupation. These categories do not apply in this decision.

"We're defining disability in general terms of being disabled, not relative to a particular occupation, or any occupation," Duddy explains. "So if someone was to lose both their legs in a car accident, that member is permanently disabled in the traditional sense, even though in the months or years that follow they may be able to work if they find an occupation that doesn't require them to use their legs.

"So the definition differs quite significantly from underwritten disability insurance that members may also be exposed to," he adds. "You could have situations where your retirement fund is willing to accept early retirement based on disability, even though you don't qualify under your insurance policy."

Moneyweb | 30 October 2018 | Patrick Cairns

How does Tax impact retirement savings

Despite the tax benefits on retirement contributions and the tax-free growth, the fact that pension income benefits are ultimately taxed has led people to question whether saving in a retirement fund really is better than making your own retirement savings arrangements with after-tax earnings.

One of the main ways government encourages people to save for retirement is to offer tax deductions on saving in an approved retirement fund.

While this tax relief can be very helpful when you're working and contributing to a retirement savings fund, the benefits that you eventually receive from your retirement fund when you stop working are still taxed.

To help South Africans make informed retirement saving decisions, Old Mutual Corporate Consultants conducted a thorough investigation into how tax impacts retirement outcomes.

The analysis aimed to compare the tax impact of various vehicles to save for retirement. The three vehicles considered were a retirement fund, discretionary savings, i.e. using after-tax income, and finally a Tax-Free Savings Account (TFSA).

Five different scenarios (using different combinations of these three vehicles) were compared:
Scenario 1: Discretionary savings only (Discretionary)
Scenario 2: Discretionary savings, but including saving in a Tax-Free Savings Account (Discretionary TFSA)
Scenario 3: Saving in an approved retirement vehicle (Retirement)
Scenario 4: Saving in an approved retirement vehicle and also reinvesting any tax savings on a discretionary basis (Retirement Plus)
Scenario 5: Saving in an approved retirement vehicle, and reinvesting any tax savings in a Tax-Free Savings Account as well as in a fully taxed, discretionary vehicle (Retirement Plus TFSA)
The analysis also considered different levels of income, because the impact of tax depends on how much you earn.
"People who earn higher salaries pay more tax, which means the different tax treatment of the savings vehicles results in more significant impacts for higher income earners," explains Andrew Davison, Head of Advice at Old Mutual Corporate Consultants. Three levels of pre-tax income were compared: R20 000 per month, R60 000 per month and R120 000 per month. ***Full Report*:** **https://www.iol.co.za/personal-finance/tax/how-does-tax-impact-retirement-savings-17701742**

Personal Finance | 30 October 2018

Financial decisions you need to make at retirement

There are a number of important financial decisions you need to make when you retire. They are:
1. What financial options do I have when I reach retirement age as stipulated by my employer?
You no longer have to retire from your retirement fund when you retire from the service of your employer and start earning a pension immediately; you may elect to retire from the fund after normal retirement age as set out in your fund's rules. This means that you will retire from your employer at your normal retirement age, but you can keep your retirement savings invested in the employer's fund until you choose to receive the money that you have invested during your working lifetime.

You can elect to defer your benefit in your current employer's fund on retirement, but you won't be able to make any further contributions to the fund. This is what you should consider when deferring your benefit:

Decide on the date you want to collect your retirement savings from the fund.
You won't be covered for the fund's insured benefits.

Your retirement savings will stay invested in the fund and you will remain invested in the investment portfolio you were invested in at retirement date.

You will continue to have the same range of investment choice.

There will still be investment fees and administration costs.

Positive and negative investment returns will be added to, or deducted from, your investment in the fund until your deferral date.

If you choose to defer outside of the fund by using personal retirement annuity (RA) funds, you can also elect to make additional contributions. This will allow you to build on the savings already accumulated.

3. What pension options are available in the market?

A pension, or annuity, is paid to you once you decide to retire. This annuity can be received monthly, but you may elect to receive it semi-annually or annually.

Guaranteed, or life, annuities pay you a pension for the rest of your life and there is no risk associated with poor market returns, because the company from which you purchased your guaranteed annuity assumes this risk.

The amount and frequency of the payment chosen at onset remains fixed throughout the lifespan of the annuitant, and unless you choose a guaranteed annuity that has some sort of inflation protection, your buying power will reduce significantly over the years, and in the case of a level annuity, the amount of income at the beginning of the annuity remains fixed. There are, however, a myriad different guaranteed annuities, and it is wise to find out about strengths and weaknesses of each.

Living annuities are more flexible, because you can draw between 2.5% and 17.5% a year and you can change the percentage and draw date of your pension on an annual basis. The downside, however, is that you are still invested in the market and assume the risk associated with poor market returns over time, and the reality of being invested in this kind of annuity is that, potentially, you may run out of money if you draw too much too soon. ***Full Report:*** ***https://www.iol.co.za/personal-finance/retirement/financial-decisions-you-need-to-make-at-retirement-17684660***

Persona Finance | 29 October 2018 | Gary Fisher

Investec’s Koseff own retirement plans mirrors the changing face of retirement

Retiring Chief executive of Investec Stephen Koseff states that retirees have a role to play to help future employees as it is their skills, knowledge and experience that could be utilized in the country.

“There is a whole group out there that can make a massive difference if they can apply some of their skills and experience to assist Government, State-owned Enterprises (SOE’s) and young people and help to make the country in what it can become,” said Koseff.

“Retirement is not what it used to be” might sound trite, but it certainly rings true in the 21 st century where people are living much longer, they are physically more active and stay healthier for longer. “Official” retirement could be just another step-change to a different lifestyle or career."

Investec’s Stephen Koseff is interviewed by René Grobler, Head of Investec Cash Investments, regarding his personal view on the next stage of his life.

“I don’t think that people should retire. For me, the kind of stuff that I will be doing is just going to be different” says Koseff. ” There is an ability to have a second life, from a work point of view. You need to take some things a bit easier, you can’t live with the same stress. But you can still be effective and do the things that give you satisfaction. Something that gets you up in the morning and that can make a difference to society”. Stephen will be staying on as a non-executive director at Investec remains the co-chair of the Youth Employment Services (YES) program, as well as taking on one or two external roles. He adds: “It’s not golf four days a week, not for me anyway.

Koseff emphasises that growing the economy should be a priority and Government should play the enabling role – the South African economy can grow at a rate of 5%.

“But for that to happen you have to be business-friendly. We will never get rid of inequality but with the inclusive growth, we can narrow the gap between rich and poor. Human capital – and the pool of retirees who have the skills – can play a major role in filling the skills gap that exists. Each skilled worker creates five jobs for unskilled workers.”

The future world of work

A long career in one job or role may be something of the past. Koseff believes while certain activities will be handled by artificial intelligence (AI) and robotics, there will still be a huge need for human intervention.

"You are still going to the need the human touch for many things. But what is very important is how technology enables us to do a better job. It takes away a lot of drudges and manual type work and gives us more time to do the work that humans are good at, which is the emotional intelligence side of life. For me this is the key - how are human beings going to partner with technology." ***Full Report:*** ***https://www.iol.co.za/personal-finance/retirement/investecs-koseff-own-retirement-plans-mirrors-the-changing-face-of-retirement-17716746***

Persona Finance | 31 October 2018

So far so good when it comes to RDR

On 18 October, FAnews published a newsletter that discussed the Phase I and Phase II implementation of the Retail Distribution Review (RDR). The newsletter generated a lot of interest among our readers with one saying that the newsletter was timeous bearing in mind the changes that are taking place in the industry.

We spoke to Lizl Budhram, Head of Advice for Old Mutual Personal Finance, to gain an industry perspective on how the RDR changes are impacting the industry.

Key focal areas

RDR has caused some measure of trepidation in the industry with some financial advisers worrying what the future had in store for them. On the other side of the coin, RDR has also added significant value to the industry in that the nature of financial advice has been formalised in ways that have never been seen before.

Phase I of RDR introduced class of business training, product training and continuous professional development (CDP) requirements which many industry role players have said is a breath of fresh air to the industry.

"Several advisers have the above elements in place in their business already, so meeting the requirements set out by the Financial Sector Conduct Authority (FSCA) will not be a problem," said Budhram, adding that advisers who have not yet met the requirements set out by the FSCA have until 2019 to do so.

She added that there has also been a lot of changes with regards to how the FSCA interacts and communicates issues with the industry. "The industry is still negotiating with the FSCA on a number of issues. This is being done through discussion papers and input that the industry provides to them. Ultimately, both parties are committed to managing the changes brought about by RDR and making sure that these changes benefit the industry and the clients that we serve," said Budhram.

Still some nervousness

Budhram was very complimentary in the way that the FSCA implemented RDR. She pointed out that the phased approach is giving the industry some sense of calm that they will not be overwhelmed as there are still some issues that are sensitive in nature.

“There still needs to be some discussion on adviser categorisation going forward. There is currently a great debate in the industry with regards to this. One of the proposals on the table is that tied advisers will be referred to as product supplier agents. There is a lot of resistance to this from the industry because advisers do not want to be seen as product pushers or product sales people. They have been painstakingly working very hard for clients not to see them in this way,” said Budhram.

There is also a debate with regards to independent advisers. Budhram pointed our that there are two possible categories on the table and that the use of the word independent in their job title still needs to be determined.

Changing focus

Initially, there was a lot of concern within the industry that RDR would cause unintended consequences which would ultimately become very detrimental. One of these fears was that advisers would begin to focus on providing financial advice to clients who could afford to pay for continued engagement. This would create a massive advice gap in the industry as not everybody would be able to afford this.

“The above situation was very much the case when RDR was implemented in England. South Africa is in the very fortunate position that it can learn from the mistakes that occurred in international markets,” said Budhram.

She added that assuming that advisers would only focus on clients who could afford to pay for continued engagement is premature. “If we look at the actuarial modelling when it comes to the final recommendations on the lower income market, the FSCA has acknowledged that fees will not be wholly appropriate in this market and that some form of commission will have to come into play. This still needs to be finalised by the FSCA and will be communicated to the industry,” said Budhram.

Focus on communication

One of the positive aspects regarding the implementation of RDR is that the FSCA is going to great lengths to communicate with the industry regarding changes that affect them.

“The FSCA has learned from its past experiences. When the FSCA made changes to FAIS Fit & Proper Requirements, the legislation was not clear with regards on how it will impact all categories of advisers. This created a lot of confusion as to who would comply with what. The industry then contacted the FSCA and asked for clarity, which came very late. The industry and the regulator needs to make sure that when legislation is promulgated, it is clear and that if there are any questions, they can be answered and clarified within the ambit of a particular Act. Currently, the FSCA is trying to live up to these expectations," said Budhram.

The fears that the industry used to have regarding RDR have not come to pass. This does not mean that it will not come to pass in the future, but the fact that the FSCA is trying its best to prevent this from becoming a reality is encouraging. ***Full Report:***
https://www.fanews.co.za/article/abc-of-rdr-retail-distribution-review/1364/general/1368/so-far-so-good-when-it-comes-to-rdr/25690

FA News Finance | 30 October 2018 | Jonathan Fourie

Why women are better investors – Study

When it comes to industries, Wall Street is about as male-dominated as they come. So many people just assume that men are better investors.

And they would be wrong.

According to new data from financial services giant Fidelity Investments, women are actually superior investors. In sifting through more than 8 million investment accounts, Fidelity discovered that women not only save more than men, 0.4 percent, their investments earn more annually, also 0.4 percent.

"It is a double whammy," says Alexandra Taussig, Fidelity's senior vice president for women investors. "The myth that men are better investors is just that - a myth."

Those differences may seem slight at first. But extrapolated over a lifetime of saving and investing, the disparity at retirement age is anything but minor. For a 22-year-old starting out with a salary of $50 000 a year, a woman investor will outpace her male counterpart by more than $250 000.

Even more revealing about general attitudes is Fidelity's companion "Women and Money" survey, which asked participants which gender was better at investing its money. The outcome: Barely 9 percent of people said women. What is it, exactly, that makes women better investors? One factor, Fidelity said, is that men are 35 percent more likely to make trades, which means that trading fees eat away at their portfolios more than they do women's. Another advantage: Women assume less risk, such as not loading up entirely on equities. They also invest more in vehicles like target-date funds, whose automatic allocations make for smarter diversification, Fidelity said.

The resulting gender outperformance gibes with a study by academics Terrance Odean (University of California, Berkeley) and Brad Barber (University of California, Davis), who also found that women outperform men, by roughly 1 percent a year. If you want to invest like a wonder woman, that means shifting to a long-term focus, saving more up front and giving up on trying to time the market with brilliant trades. "Men regard their stock picks as a sport that comes with bragging rights, and that is what gets them into trouble," said George Gagliardi, a financial planner in Lexington, Massachusetts.

Personal Finance
30 October 2018

How to improve SA's pension system

South Africa can improve its pension system by introducing a minimum level of compulsory contributions to retirement savings vehicles or increasing the level of preservation when members change jobs.

This is according to the 10th Annual Melbourne Mercer Global Pension Index, which benchmarks the retirement income systems of 34 countries against roughly 40 indicators.
While South Africa scored relatively well with regard to the integrity of its retirement income system, the research raises questions about the adequacy and sustainability thereof and gives the country an overall score of 52.7 (C grading). This puts its performance on par with nations like the US, Brazil, Spain, Italy and Indonesia. The only two countries to receive an A grade in 2018 were the Netherlands with a score of 80.3 and Denmark (80.2).

South Africa has been on a gradual yet rocky road with regard to retirement reform, as many pensioners struggle to make ends meet. New regulations will require retirement funds to implement a default investment, preservation and annuity strategy by March 1, 2019, which should lead to better retirement outcomes for some members, but the country's high unemployment and low economic growth rate have hindered reform efforts and attempts to introduce compulsory annuitisation in the provident fund space have effectively stalled.

"South Africa's pension system is well regulated and demonstrates overall good governance, which impacts the level of confidence that South Africans have in the system," says Nicolette Hendricks, CEO of Mercer South Africa. "Considering that the primary objective of any pension system is to provide adequate retirement income, ours falls short when looking at the adequacy of benefits and sustainability of the existing retirement income system."

Substantial government debt, slow economic growth and no minimum level of mandatory contribution levels designed to provide adequate retirement income are some of the risks and shortcomings observed. It's equally important to note that home ownership represents an important feature of financial security in retirement, she adds.

Dr David Knox, senior partner at Mercer Australia and author of the study, says the natural starting place for a world class pension system is ensuring the right balance between adequacy and sustainability.

"It's a challenge that policymakers are grappling with," he says. "For example, a system providing very generous benefits in the short term is unlikely to be sustainable, whereas a system that is sustainable over many years could be providing very modest benefits. The question is – what's an appropriate trade-off?"

To improve its overall score, the researchers recommend that South Africa increase the minimum level of support for the poorest pensioners and increase the coverage of employees in occupational pension schemes (thereby increasing the level of contributions and assets).

They also recommend that South Africa introduce a requirement that part of the retirement benefit from provident fund arrangements be taken as an income in retirement (this already applies to pension funds and retirement annuities). The introduction of compulsory annuitisation for provident funds was previously postponed by another year to March 1, 2019 to allow for further consultation.

Hendricks says every country has its own unique economic, social and political circumstances but can still take steps to improve their pension system. "In the long term, there is no perfect system, but the principles of 'best practice' are clear."

She adds that pension systems should be looking at a range of reforms that can be implemented to improve the long-term outcomes, such as encouraging higher levels of saving, reducing the leakage from the retirement savings system prior to retirement when changing jobs, improving governance, and introducing greater transparency to improve the confidence of members.

David Anderson, president of international at Mercer, says that as people are increasingly living longer, it is positive to see governments take steps to reform their pension systems.

Moneyweb | 23 October 2018 | Ingé Lamprecht

INTERNATIONAL NEWS

401(k) rule change would ease small companies’ path to joint plans

Our daily roundup of retirement news your clients may be thinking about.

401(k) rule change would ease small companies’ path to joint plans
Small businesses would find it easier to offer 401(k) plans to their workers to help them prepare for retirement under the regulation proposed by the Labor Department, according to this article on The Wall Street Journal. The proposed rule would allow small companies with a common owner or from the same industry trade group to band together and create multi-employer retirement plans. Creating multiemployer plans would enable companies to reduce administrative and investment fees.

How will a couple’s retirement look when there’s a big age gap?
Age gaps between spouses can be a crucial factor when they start planning for retirement, according to this article from *The Washington Post*. The age gap should be considered when making financial decisions, such as the age to retire and to file Social Security as well as planning how to save and invest for the golden years, according to the article. “Especially if the younger partner is a woman, an age difference can mean you need your money to last longer. Women outlive men on average, which adds additional years to retirement.”

Whose record will my Social Security benefit be based on?
A wife who intends to file for Social Security when she reaches full retirement age will receive whichever is higher between her Primary Insurance Amount and 50% of her husband's PIA, if her spouse is already on Social Security, according to this Q&A article on Forbes. If her husband hasn't filed for his own retirement benefit at the time she submits her application, she will receive her own retirement benefit and may later on get additional benefit once the husband starts collecting his own retirement benefit.

There's no magic number for self-funding long-term care
Clients who opt for self-funding long-term care are likely to save more, as the cost is increasing faster than inflation, writes an expert for Morningstar. "To gauge asset adequacy for long-term care costs, the first step should be to make a reasonable estimate of what those expenses might be," writes the expert. "Then, armed with a view of those expenses, you can assess whether the amount that's left over in your portfolio after you've covered your other expenses is sufficient to fund them."

Financial Planning | 23 October 2018 | Lee Conrad

The difference between the best and worst superannuation funds

AUSTRALIANS could be missing out on tens of thousands of dollars or the equivalent of multiple round-the-world tickets. AUSTRALIANS could be costing themselves tens of thousands of dollars of savings, the equivalent of multiple round-the-world trips, in retirement by signing up to the wrong super fund. Many bank-owned super funds were given a hiding in the recent financial services Royal Commission for failing to do the right thing by customers.

This included charging members high fees, giving conflicted financial advice and consistently delivering poor returns. New analysis by roboadviser Stockspot, in its latest Fat Cat Funds Report looked at hundreds of super funds, including their fees and performance over the past five years. It found a 30-year-old male could end up with $544,000 if they retired at 67 and invested their money in some of the best balanced super funds.

This compared with $470,000 at retirement if they had some of the worst funds with higher fees and poor returns. According to Stockspot's methodology, a balanced super fund typically invests around 40 to 60 per cent in shares and property. Stockspot found that for balanced funds, the top 10 had average fees of 1.05 per cent and returns of 7.75 per cent over the past five years. The worst funds had average fees of 1.47 per cent and returns of 4.86 per cent.

Australian News | 23 October 2018 | Sophie Elsworth

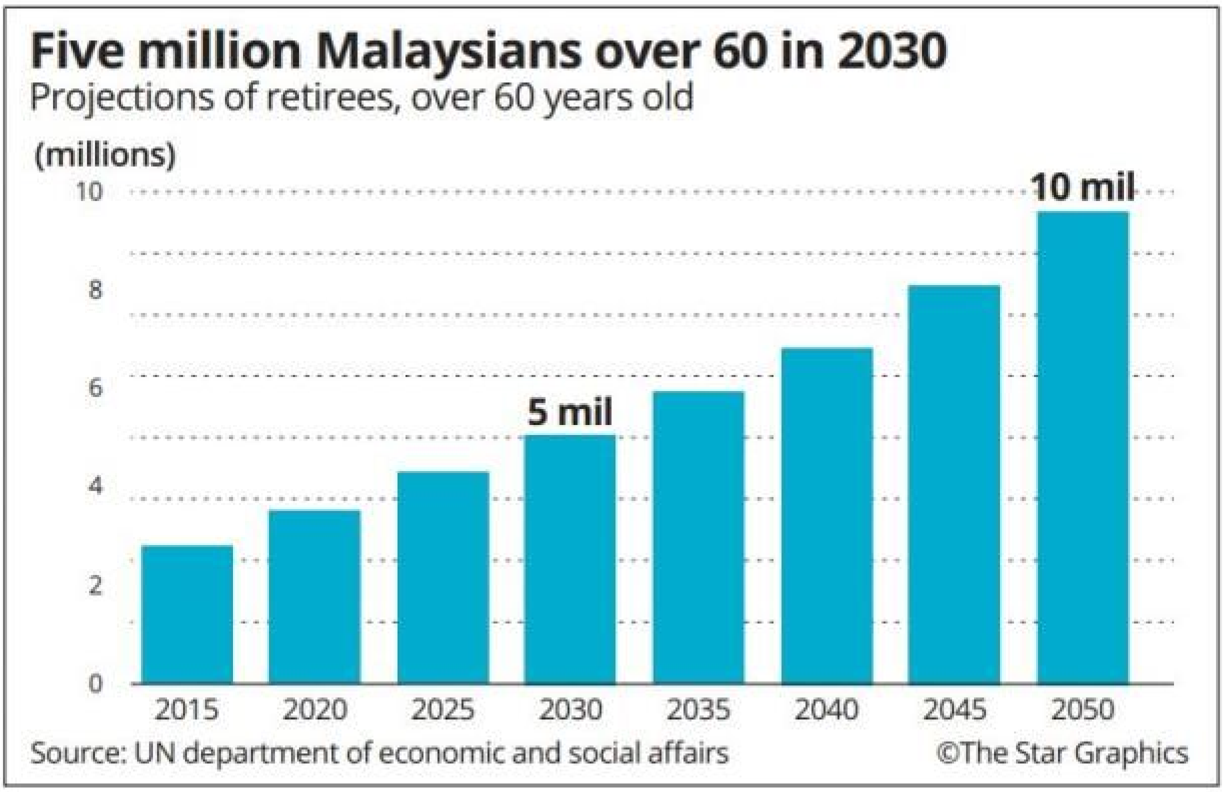
Are retirement schemes sufficient for Malaysians?

FINANCIAL security in old age has never been more important, what with declining birth rates and increasing longevity.

For many Malaysians and Asians who in the past used to depend on their children and grandchildren as a primary source of income post retirement, the pressure is increasing as people are living longer but having fewer children to support them. Not surprisingly, retirement income systems worldwide are under pressure.

Mercer, a leading global professional services firm, recently launched its annual Melbourne Mercer Global Pension Index (MMGPI), revealing important information on how some 34 countries are preparing for tomorrow's ageing world.

Among the 34 pension systems measured, there is wide gap among the systems around the world with scores ranging from 39.2 for Argentina to 80.3 for The Netherlands. The Netherlands and Denmark come up tops (with scores of 80.3 and 80.2 respectively), both offer A-grade world class retirement income systems with good benefits.



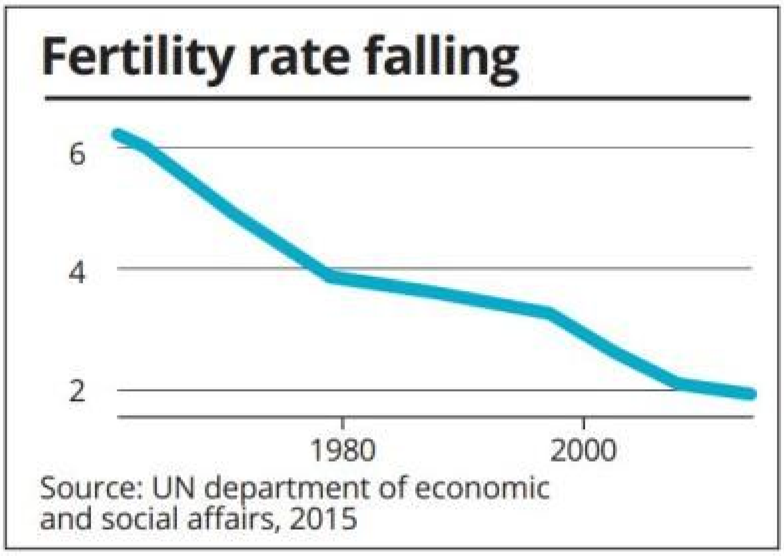
The index indicated that Malaysia maintained a stable C rating, compared to some Asian countries, coming up ahead of Japan and South Korea, but behind Singapore. On Malaysia's Global Pension Index score, Mercer Malaysia CEO Hash Piperdy says: "Malaysia maintains a stable C rating but action needs to be taken to address our ageing nation – over five million Malaysians are expected to be over 60 years old by 2030, and nearly 10 million will be over 60 by 2050.

"Malaysia's sustainability score has decreased from 61.2 to 60.5, based on the index. There still exists a gap which poses risks in terms of the long-term sustainability in the system due to the ageing population, and the need to address it is crucial as there are still many Malaysians without sufficient pension savings on top of the Employees Provident Fund (EPF). It is high time for industry and community groups to look into Private Retirement Schemes (PRS) and other ways to boost long-term savings," he adds.

Malaysia's retirement income system is predominantly based on the EPF which covers all private sector employees and non-pensionable public sector employees. Under the EPF, some benefits are available to be withdrawn at any time (under pre-defined circumstances including fund education, home loans, or severe ill health) with other benefits preserved for retirement.

Introduced in 1951, the scheme makes it compulsory for employees to contribute 11% of their salary towards their personal EPF account. Employers are also required to contribute 13% of the salary for employees earning RM5,000 and below, and 12% if the employee's salary is more than RM5,000.

Although the guaranteed base dividend rate for EPF is 2.5% per annum, Malaysians have been enjoying an average 6.02% for the last 10 years (2008-2017). This high EPF dividend rate has given many Malaysians a false sense of long-lasting financial security.



The institution suggests that the minimum savings EPF members should have at age 55 is RM228,000. This equates to a monthly withdrawal of RM950 to cover basic needs for 20 years. However, according to a 2016 survey by the Department of Statistics Malaysia, the average household expenditure of Malaysians was RM4,033.

EPF reported that only 18% of members have the minimum savings target of RM228,000 in their account by 55.

Mercer points out that the overall index value for the Malaysian system can be increased by:

> Increasing the minimum level of support for the poorest aged individuals;

> Raising the level of household saving and lowering the level of household debt;

> Introducing a requirement that part of the retirement benefit must be taken as an income stream; and

> Increasing the pension age as life expectancy continues to increase.

Making good progress

Piperdy says a well-functioning social security system is needed, one where an income stream is provided rather than just a lump sum payment upon retirement.

"This could be something like the CPF Lifelong Income For The Elderly (CPF LIFE) scheme that they have introduced in Singapore. By having this, people don't outlive their savings and there is less reliance on family support. However you have to build up that nest egg before you can drawdown on it," he says.

Piperdy commended the EPF's efforts and said that there are already a lot of good steps being taken, and there is still time to improve on the system. However, there are fundamental changes that need to made because the population is aging fast.

"Aging is accelerating. Some 20 to 30 years ago, Malaysians used to have families with 6 to 7 children, but now its under 2 children. This is definitely going to create pressure," he says.

He said that people are now expected to live on average for another 20 years after they retire.

In recent years, there has been an increasing trend where people do not withdraw their EPF in one go.

"The beauty of drawing down this way is that the remaining money in the EPF benefits from the dividends," he says.

The other issue is an older retirement age.

Piperdy says that as people are living longer today, it is important to have more flexible retirement ages. After all, the economy is changing and people don't stay with the same company for most of their lives anymore.

"Instead of having a hard cut-off at 55 or 60, perhaps we could have flexible retirement so that an individual can carry on working while concurrently drawing down on their EPF, before gradually moving on to full retirement."

"If you are 55 today, try not to withdraw your entire EPF savings in one lump sum. You can also defer the age where you stop working. Just by contributing a little bit more, that money goes very far – you will be drawing down on that extra contribution for the next 20 years. These small steps can make a big difference," says Piperdy.

Multiple sources

Piperdy says that to have that income stream, one must build up on one's nest egg so that there is a decent amount first.

"To build it up, this simply means more contributions. One way is via the PRS. In an A-rated or a high B-rated pension system, an individual has multiple sources of contributions.

"The Netherlands and Denmark have multi-tiered retirement plans. For example they have social security scheme which provides a basic income for everybody. That is supplemented by company pension plans.

"So perhaps the social security part covers 10% to 15% of retirees' needs, while a further 30% to 40% comes from company pension plans. The remainder comes from private savings or investments," he says.

In Malaysia, it is still the EPF that most people rely on. Piperdy feels there are opportunities to develop more company pension plans as the infrastructure is alredy in place. "The Securities Commission and the government introduced the PRS a few years ago. Its got some RM2bil in assets, and has been successful so fast, although it is on a voluntary basis. I would like to see more incentives for employers to set up these plans for their staff," he says.

For some background, the PRS is a voluntary long-term savings and investment scheme designed to help individuals save more for their retirement.

Each PRS offers a choice of retirement funds from which individuals may choose to invest in based on their own retirement needs, goals and risk appetite. The fund options under PRS are intended to enhance long-term returns for members within a regulated framework.

The year 2017 was a record year for the PRS, attracting the highest number of new members to the savings fund since its launch five years ago. Total members grew by 36% to 301,279 in 2017, from 221,235 in 2016.

Meanwhile total asset under management (AUM) of the 56 existing PRS funds rose by 47% to close the year at RM2.23bil, from RM1.51bil in the year before. Piperdy would suggest eventually having auto-enrollment of these savings plans as one way to broaden the contribution base.

"Everyone complains that money is tight, but who is going to miss 1% of their salary.If that 1% increases to 2% in a few years, that makes a huge difference later on in life," he says.

Holistic approach

Author of the study and senior partner at Mercer Australia, David Knox says that the natural starting place to having a world class pension system is ensuring the right balance between adequacy and sustainability.

"It's a challenge that policymakers are grappling with. For example, a system providing very generous benefits in the short-term is unlikely to be sustainable, whereas a system that is sustainable over many years could be providing very modest benefits. The question is – what's an appropriate trade-off?" he says.

Knox adds that it's not enough for a system to be sustainable or adequate. In some countries, broad coverage has been successfully accomplished through compulsory workplace pension systems or in some cases, auto-enrolment arrangements. ***Full Report: https://www.thestar.com.my/business/business-news/2018/10/27/are-retirement-schemes-sufficient-for-malaysians/***

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