FRIDAY, 19 AUGUST 2022

irfa dispatch

THE RETIREMENT INDUSTRY NEWSLETTER

TABLE OF CONTENT

LOCAL NEWS

Simplifying the complexities of retirement annuities

It's important to know the difference between pre-retirement- and during-retirement vehicles that allow a sustainable monthly income.

The future looks bright for the next generation of retirees – we're living longer, with the number of South African centenarians increasing every year. It is expected that Africa's population of older adults will more than triple, from 46 million in 2015 to 157 million by 2030 (WHO 2015). We're also approaching retirement age with a greater sense of purpose. This longevity requires us to deliberately think about ways of funding our retirement. With more life to look forward to and more passions to pursue, it's essential that we build a nest egg that lasts our full lifetime. This is where annuities come in. Over the years, the various types of annuities have attracted both fans and critics through a variety of perceptions and misconceptions. Let's debunk a few of the more common myths about annuities.

Debunking myths

The word 'annuity' is used in different ways in financial products so it can appear complex. It is important to understand what each of them mean so that it is clear where and when to use them. A *retirement annuity* is a savings vehicle that offers a very tax efficient way of saving towards retirement. In this type of product, a client contributes regularly, and the money grows in the investment components that they choose. The aim is to accumulate as much as possible to be able to get a higher income during retirement.

Retirement annuities are a common means of savings, in tandem to retirement vehicles like pension and provident funds made available by an employer. It is also the most effective way for self-employed people to save towards their retirement. The important part is that you use a retirement annuity to *save* for retirement. At retirement, part of the accumulated retirement savings must be converted into an income stream. There are two broad types of annuity products used to provide an income *during* retirement.

Living annuities are market-linked investments designed to give clients a regular retirement income, while simultaneously aiming to grow their retirement savings. A small portion is withdrawn from their retirement savings each month to provide them with a regular income. The market value of the living annuity will vary, depending on the performance of the underlying investment portfolios, and the level of income they withdraw every month.

Life annuities pay a regular income for life to the client, protecting them against market fluctuations. The insurer guarantees that the income you receive will never reduce for as long as you live, so you can't outlive your income. This type of an annuity is typically ideal to match one's basic life expenses such as medical costs, groceries and other regular essential spending. There is a better way for people to, together with their financial adviser, plan and structure their finances when they retire to blend their need for certainty and flexibility. A combination of a life and living annuities can provide the best of both worlds.

As market volatility and inflation continue to rise, it's crucial for clients to gain a full understanding of a process that may occupy them most of their lives. Clients need to understand the importance of contributing towards their retirement while they are employed and earn an income. The more you contribute and the higher your growth rates, the more you will be able to 'earn' during your retirement. It is important to know the difference between pre-retirement vehicles and during retirement vehicles that allow one to have a sustainable monthly income. Contact a financial adviser to truly understand the benefits and functionality of annuities on your journey to success.

Moneyweb | 13 August 2022

Only 480 pay-cheques to go until retirement: Better get started!

If you think you have thousands of paydays until retirement, think again. At age 25, with a retirement age of 65, you can expect just 480 more pay-cheques until retirement, at 35 around 360, at 45 around 240, at 55 around 120… "Thinking of your income as finite can be a wakeup call and is a very good reason to make every single month count," says Karen Wentzel, Head of Annuities at Sanlam Corporate. Unfortunately, most South Africans are not able to retire comfortably.

Not starting to save for retirement early enough is a key reason for this. "It really is imperative to start young, if possible, and save what you can – small amounts make a massive difference thanks to the magic of compound interest," says Wentzel. Making every single pay-cheque count – both to save for the years when you won't be working and to save for big life events like buying property – is an extremely astute way to build wealth and live a life of confidence.

A FORMULA FOR SUCCESS

Wentzel breaks down the percentage of a pay-cheque to try to save at various ages, plus the pros and cons of some savings vehicles. "An easy way to understand how much to save is to consider your retirement savings as a multiple of your current salary at different points in your life. The goal is to have a multiple of 15 times your annual salary saved at retirement." For example, if you've worked for five years and earn R240 000 per annum, you should have a multiple of 1.2 times your current annual salary saved, totalling R288 000.

Years worked	Multiple of current salary saved
5	1.2
10	2.3
15	3.7
20	5.3
25	7.2
30	9.4
35	12.0
40	15.0

This table is calculated on the assumption that you retire at 65, save 15% per annum of your annual salary (including an annual bonus), and earn investment returns of 10% a year, with salary increases of 6.5% each year.

Wentzel cautions that 15 is more than a number. For example, for each million that a 65-year-old saves, a male will receive a monthly pension of about R7 000 per month and a woman – due to her longer life expectancy – will get R6 000, growing with inflation each year. So, a person needs to save 15 times their final salary to afford an inflation-linked annuity at age 65.

What to do when switching jobs?

In the instance of unemployment or when switching jobs, the most important rule is to not withdraw your money, but to preserve it in a preservation fund. Once you cash out your savings, tax is payable if the savings exceed the tax-free limit. You'll need to contribute much more each month to play catch up if you start saving later. Here's the percentage of your salary you'll need to save:

Start saving at age	Percentage of salary needed to save
25	15%
35	24%
45	43%
50	60%

So, if you cash out your retirement savings at age 45, you will need to contribute 43% of your savings when you start a job again (at age 45) to retire at age 65 with financial freedom.

What if you're self-employed?

If you're self-employed with unpredictable pay-cheques, consider committing to a lower percentage saving in your provident fund, e.g., 10%, and try to save the extra 5% in other, more flexible financial vehicles where your contributions can fluctuate. You may also consider building up a share portfolio. Make sure to make full use of the tax advantage of investing up to 27.5% or R350 000 per year.

Sidebars:

Choosing the right vehicles to supplement your retirement savings is very important. In addition to a traditional pension or provident fund or retirement annuity, it may well be worth exploring these options:

• tax-free investments

• unit trusts

• online share account or a

• government retail bonds

Here are the advantages and disadvantages of alternative products:

Tax Free Investments

These were introduced in March 2015 as an incentive to encourage household savings.

Pros:

- No income tax, dividends tax or capital gains tax on the returns from these investments.
- A range of investments are available including investments in fixed deposits, unit trusts (collective investment schemes), retail savings bonds, linked investment products and exchange traded funds (ETFs) that are classified as collective investment schemes

Cons:

- You can only contribute a maximum of R36 000 per tax year (annual limit)
- There is a lifetime limit of R500 000 per person
- If a person exceeds the limits, there is a penalty of 40% of the excess amount

Unit trusts

These are portfolios of assets – for example equities, bonds, cash, and listed property – in which investors can buy units. This investment vehicle allows investors to spread their risk, whilst getting the benefits of professional fund management.

Pros:

- Unit trusts are flexible investments with a wide variety of option to invest in
- It helps with diversification of investments and allows 100% investment in equities
- Unit trusts can be set up as a regular savings programme

- Your resources are pooled with other investors, allowing you to make investments impossible as an individual investor

- You get the benefits of greater economies of scale, such as reduced transaction costs

Cons:

- There are costs over and above those you'd pay if you were investing directly

- No tax incentive on unit trusts

An online share account

This is an investment platform for trading (buying/selling) financial securities or currencies with the use of a brokerage's internet-based trading platform.

Pros:

- Easy access to trading shares in real-time

- It is easy to open and manage an account without geographical limitations

Cons:

- Online trading is risky if the investor doesn’t have adequate knowledge of financial markets

- No tax incentive on unit trusts

Government retail bonds

These are a low-cost way to buy bonds, with one of the advantages being that the investment can be as low as R1000, with the investment term being 2,3 or 5 years. Inflation-linked government retail bonds are also available for investors who are worried about inflation.

Pros:

- Government retail bonds are a low-risk investment option as you are lending money to the government, with the chances of the South African government defaulting on this loan being low

- Retail bonds are easy to buy on the government retail bond’s website, or via the Post Office, branches of Pick n Pay or over the phone.

- The return on government retail bonds is known in advance, which means you can anticipate what income to expect over the term

Cons:

- No tax incentive on retail bonds except if it is part of a tax-free savings account. ***Full Report: https://www.fanews.co.za/article/retirement/1357/general/1358/only-480-pay-cheques-to-go-until-retirement-better-get-started/35219***

FA News | 16 August 2022

SME employees not saving enough for retirement

On the back of the widely known statistic that over 90% of South Africans are not in a position to retire comfortably, FNB Employee Benefits has also noted a growing trend amongst SME employees not fully understanding or saving enough for retirement. “Although up to 70% of our commercial banking employers currently don’t offer formal benefits to their staff members, the small and medium businesses that do offer these benefits are concerned at the low rate of retirement saving from their staff. Poor savings and over-indebtedness often result in several work-related challenges including poor performance and job hopping.

On the positive side, employees who better manage their personal finances tend to be more satisfied, motivated, and productive,” says Elize Giese, FNB Employee Benefits CEO. “As part of broader initiatives to improve South Africans’ savings habits, SMEs too have an important role to play: Employers should consider investing in improving money management amongst their employees as part of their employee benefits offering,” adds Giese as she unpacks some of the reasons for employees’ lack of savings for retirement:

• **Preservation when changing jobs – if people change jobs and have existing retirement savings** from the previous employer, employees are urged to preserve their retirement savings. Sadly, in South Africa it is popular to cash in retirement savings when changing jobs and this is one of the reasons so few people can afford to retire. This has a double impact - you spend the money that is meant for retirement and more importantly, you lose out on the growth and compounding of the money over time. This has a much bigger impact than most people realise.

Consider this example: you pay R1 000 per month into your fund and earn a net 4% real return (after costs and inflation). Over forty years this investment would grow to R1.14m. But after ten years you change jobs and decide to upgrade your car with your savings, and to start saving afresh. At that point your investment is worth R144 000. As a consequence of this decision, at retirement you will only have saved R673 000. This is 41% less than before. That means a 41% lower pension! That car upgrade actually cost you R467 000, and possibly a comfortable retirement.

• **It’s impossible/too late to secure a financially comfortable retirement –** answer is simple, the sooner the better, even contributing a small amount to retirement savings now can be very beneficial in the long run.
• **Lack of understanding of benefits -** financial literacy among the general public continues to be low, and monetary worries remain a common source of stress, absenteeism, and poor

performance at work. Employers need –now more than ever– to focus on improving the financial education of their employees. They must help staff gain the confidence to improve their financial wellbeing, and the confidence to face changes, both in their personal circumstances and the wider economy, without losing their focus at work. Lastly, there's a common misconception amongst employees that all savings are the same. One of the key reasons for this is the fact that educational material shared by SMEs does not adequately highlight the importance of understanding that not all savings are created the same.

"By lumping retirement savings, fixed-term and call accounts, day-to-day savings vehicles, emergency savings, tax-free savings and even many forms of investment together under the banner of 'savings', a misperception has been created that all these savings vehicles are the same. The result is that many employees don't realise that each type of savings account has a very unique purpose and requires a different mindset in order to deliver on that purpose," concludes Giese.

FA News | 16 August 2022

5 steps to a comfortable retirement

According to the South African Treasury, only 6 out of every 100 South Africans will be able to retire comfortably. And a **recent BusinessTech poll** shows more than a third (35%) of middle-class South Africans aren't putting any money at all away for their retirement. As a result, growing numbers of consumers are turning to direct investments on online trading platforms to try and boost their retirement savings – but it's a high-risk strategy that ignores the fundamentals of proper retirement planning, says Dieter Schmikl, a financial advisor at employee benefits firm NMG Benefits. "As more consumers get educated and digital, we hear many stories of people making quick money trading forex or shares online. But that's not how you plan for retirement. The fact is that if something sounds too good to be true, it probably is," says Schmikl. So how do you get yourself on the road to good financial health and a comfortable retirement? It's a smart, measured five-step process that looks after your priorities.

Step 1: Spend less than you earn

"Find a lifestyle that gives you the capacity to breathe financially, and to enjoy the quality of life that you're looking for, with some money left over every month to save or put away for your retirement," says Schmikl.

Step 2: Take care of risk

If you can't earn an income because of injury or illness, who's going to pay your bills and monthly obligations? Before you save for anything else, make sure you have income protection in place. It’s a critical part of any balanced financial plan, with a long-term view to a secure retirement.

Step 3: Make provision for retirement

The biggest reasons that most South Africans can’t retire comfortably is that they start putting away money too late for their retirement, or they don’t put the right amounts away. “Retirement funding is a numbers game. It’s critical to sit down with an advisor and work out how much money you’ll need in your retirement, how much you’ve got, and what the difference is,” says Schmikl. The rule of thumb is that of you start putting away 15% of your earnings at the age of 28, you’ll be able to retire comfortably at 65, with 75% of your earnings. The later you start, the higher this percentage gets.

If you don’t have enough retirement savings, crunch the numbers. For every million rand you have in retirement savings, you’ll get around R4000 a month at sustainable draw-down levels, increasing with inflation. “Ask yourself how much you will you draw down per month to support your lifestyle. Can you put away more every month? Or do you need to carry on working for a few extra years. If your house and car are paid off, you probably need less than you think,” says Schmikl.

Step 4: Look at short-term investments

When, and only when, you have taken care of your risk and your retirement, you’ll be in a position to start looking at short-term investments, like unit trusts. But be focused on which investments you want to invest in, and try to diversify your portfolio to smooth out the bumps along the road, says Schmikl.

Step 5: If you still have money left, go high risk

We’re bombarded daily with ads that promise exponential returns through trading forex, cryptocurrency or equities. If you have some spare cash, feel free to dabble. But where many of these platforms offer high rewards, but they generally come with high risks too, warns Schmikl. “You’re not going to turn R10 000 into millions in the space of three years. That’s not how it works.” “Ultimately, retirement is all about diversification, spreading your risk and beating inflation on an annual basis. If you get that right, you’ll be able to retire comfortably at the age you choose.”

FA News | 16 August 2022

How much you need to save to retire early (or do whatever else you'll have the freedom to do)

MONEY BASICS WITH MARTIN HESSE

There is an international movement among young people called FIRE, which stands for Financial Independence, Retire Early. The goal is to save as much as you can when you are young, so that you build up a nest egg on which you can retire by the time you're in your early 40s. These people are fanatical: they recommend putting away between 50% and 70% of your salary each month. However, unless you're earning a professional salary but living like a bergie, there are very few of us, particularly now in the face of rising living costs, who would be able to do that.

But the idea is a worthwhile one. And if you make the right investment decisions and remain committed to saving a certain percentage of your salary each month (over and above what might be coming off your salary for your pension fund and what you might be paying on a mortgage bond, which in itself is an investment), your nest egg will grow remarkably quickly so that, although you may not be able to retire in your 40s, by 50 you'll have saved enough to have the financial freedom that most people only dream of.

Let's do some sums.
Say you're 25 and, after tax and retirement fund deductions, you take home R20 000 a month. For the purposes of this example, I will assume zero inflation, so you can get an idea of what your money will be worth at today's rand value. Let's say your salary, taking into account bonuses and promotions, rises by an average of 3% above inflation each year. And your savings in a high-growth investment give you a return of 7% above inflation, on average, annually. (This is a realistic after-inflation return that, over periods of 10 years or more, you could expect from an equity fund).

So in a zero-inflation world, your income would increase by 3% a year and your investment by 7% a year. If you put away 10% of your salary each month, by investing R2000 a month initially but increasing this in line with your salary increases, after 18 years you will have saved R1 million. But wait, here's the magic of compound interest: after only another seven years you will have doubled your money and will have R2 million. By this time you'll be 50 years of age. If you had also been accumulating 15% of your salary in a retirement fund, this would give you another R3 million. So you'd have R5 million (at today's rand value).

By 55, the youngest age at which you can officially retire, you will have built up a sizeable nest-egg on which to do just that: R3.3 million in your discretionary investment and R4.9 million in your retirement fund, totalling R8.2 million in all. Imagine what you could do with saving 20% of your salary!

REAL RETURNS

Real returns are what your investment gives you after inflation. In other words, if inflation was 5% and your investment gave you an 8% annual return, your real return (the percentage by which your investment increases in real value) would be 3%. If your investment gave you only a 5% return, it would not be increasing in value at all, because the buying power of your money would be decreasing at the same rate.

This is why, if you are investing for the long term (10 years or longer), you need to be invested in an asset class that, in all probability, will give you good real returns. The accompanying table, provided by Old Mutual Investment Group in its latest Long Term Perspectives report on long-term investing, shows the real returns of the different asset classes as well as those of a typical "balanced fund". As you can see from the table, equities (shares in companies) – both South African and global – have yielded the highest real returns over very long periods.

REAL RETURNS	ANNUAL RETURNS					LONG-TERM RETURNS				
	2021	2020	2019	2018	2017	Last 5 yrs	Last 10 yrs	Last 20 yrs	Last 50 yrs	Last 92 yrs
SA Equity	22.2%	-3.3%	2.6%	-12.5%	15.5%	4.2%	5.5%	7.1%	7.9%	7.3%
SA Property	31.6%	-37.0%	-2.0%	-28.5%	11.9%	-8.3%	0.9%	8.4%	-	-
SA Bonds	4.2%	4.5%	6.1%	3.1%	5.2%	4.6%	3.1%	3.8%	2.6%	1.8%
SA Cash	-0.2%	1.3%	3.1%	2.7%	2.7%	1.9%	1.2%	1.9%	2.0%	0.8%
Global Equity (ZAR)	27.8%	17.6%	20.0%	2.1%	6.4%	14.4%	15.6%	4.5%	7.6%	7.6%
Global Bonds (ZAR)	-2.3%	10.8%	-0.9%	10.5%	-7.6%	1.8%	3.1%	0.5%	4.2%	3.4%
Gold (ZAR)	-0.1%	25.8%	10.7%	10.2%	-2.6%	8.4%	3.7%	5.6%	5.3%	3.9%
Balanced Index Returns	17.2%	4.6%	7.0%	-4.4%	9.6%	6.6%	7.1%	6.6%	6.9%	5.9%

If you are targeting a real return of 7% (as in my example above), the best combination of assets to give you that return would be South African and global equities, based on past performance.

Personal Finance | 16 August 2022

INTERNATIONAL NEWS

State pensioners look set to get double-digit pay rise as inflation hits 40-year high

INFLATION has hit another record high of 10.1 percent in July this year which means pensioners getting the state pension look set to receive an increase in the double figures next year, thanks to the triple lock. Inflation is at the highest figure since February 1982, when Consumer Prices Index (CPI) reached 10.4 percent, according to Office National Statistics (ONS) data, published yesterday. James Jones-Tinsley, Self-invested pensions technical specialist at Barnett Waddingham said the rate suggests the new Prime Minister faces a "pensions tightrope" come September. "The 0.9 percent rise surpasses expectations which could see inflation rise to 13 percent in the coming months.

"Calls for targeted support for the most vulnerable are already gaining pace, with pensioners, who are usually on a fixed income and have higher fuel bills, among the hardest hit. “Under the current double lock, state pension increases of the past year have been just a third of CPI, making it a struggle to maintain their standards of living. But reinstating the state pension triple lock will make life better in the short term at least. "The two-month countdown has now begun for September’s CPI figure to be released in October, which will tell us whether we could be looking at a double-digit increase come April 2023, once a decision is made on state pensions.

“But, such measures could stoke inflation further and run counter to promises of increased fiscal responsibility across the economy. This could be a bitter pill to swallow for the next Prime Minister, especially after torpedoing inflation busting pay rises for public sector workers on the same grounds.” In June 2022, the Consumer Prices Index (CPI) hit 9.4 percent. Plans to reintroduce the triple lock were reinstated by the UK government this year and is supported by both of the contenders for the Conservative party leadership Liz Truss and Rishi Sunak. The triple lock, introduced in 2010, pledges to increase the state pension by whichever is highest out of inflation, earnings or 2.5 percent.

The triple lock promise applies to both the basic state pension, pre-April 2016, and the new state pension, post-April 2016. The triple lock was suspended for one year in April 2022 as the end of the COVID-19 furlough scheme inflated average earnings growth. The government is now bringing it back in time for the annual update in pension and other benefits, which will come into effect in April 2023. For the 2022-23 tax year the full new state pension sits at £185.20 a week, or £9,630.40 for the year.

If the inflation figure in the year to September 2022 hit more than 10 percent, the value of a full basic state pension would climb past £155 a week. The new state pension would increase to more than £200 a week. The official date for an announcement on updated state pension rates is yet to be confirmed. However, it can be estimated by comparison to last year. In 2021, the new rates were announced by the Government on November 25. If the time frame is kept to it means we are likely to see confirmation of the new rates in the coming months. ***Full Report:*** ***https://www.express.co.uk/finance/personalfinance/1656291/state-pension-uk-inflation-rate-rise-increase-triple-lock***

Express | 18 August 2022

'Too big for Australia', says pension fund eyeing global expansion

SYDNEY, Aug 16 (Reuters) - Australia's biggest pension fund has outgrown the country and wants to quadruple in size to be a global investment powerhouse worth A$1 trillion ($700 billion) within a decade, its Chief Executive Officer said on Tuesday. AustralianSuper, which has A$260 billion of the country's retirement money under management, plans to invest up to 70% of its capital offshore to avoid "performance drag" by focusing on home, Paul Schroder said in a Reuters Newsmaker interview. "We are too big for Australia," Schroder told the online event. "We consider ourselves a global investor with domestic beneficiaries.

It is true we were far too Melbourne-centric and Australian orientated, but we are generally in all of our fibres taking the view that we are global investors." Australian pension fund managers have benefited from a system introduced in the 1980s under which employers must pay an additional 10.5% of staff wages as superannuation. That has left funds flush with money to invest, but with limited assets to purchase domestically. AustralianSuper now has up to 70% of its funds managed offshore, according to Schroder. The organisation had 70 staff in a London office, with plans to triple that headcount. An office in New York, which was focused on private equity investing, was also growing, Schroder said.

The fund, which owns ports, airports, rail and road infrastructure in Australia, Europe and North America, has said it wants A$500 billion in assets by 2026, but Schroder said he was taking a longer view. Within a decade, he said, "we want to be a one trillion dollar investor". "We're unashamedly in the business of scale," he said. AustralianSuper had no specific investment target but considered unlisted assets well-suited to its business in the current economic climate, since they typically carried "inflation protection", Schroder said.

At a time of economic, geopolitical and logistical disruption, Schroder said the single biggest investment challenge was inflation, and he dismissed reports that rate increases by the U.S. Federal Reserve were starting to slow the overheated economy. "You need to see some sustained signals to say it's dealt with," he said. "Our view is that there's some pretty tough times ahead. We think we're in tight environment. The question is: what's the rate of that tightening and is there a pivot around the corner?"

Reuters| 16 August 2022

Switchboard: 011 450 1670 / 081 445 8722
Fax: 011 450 1579
Email: reception@irfa.org.za
Website: www.irf.org.za

3 Williams Road
Bedfordview
Johannesburg 2008