

## INVESTING — 1

### Too easy not to save

#### Need for compulsory retirement provision

**I**N A KEYNOTE address on 13<sup>th</sup> July, at the 10th Anniversary of the South African Savings Institute and Launch of Savings Month 2011, Finance Minister, Pravin Gordhan, posed the question: 'Why don't we save?'

He cites various reasons: "People's short-term outlook, the lack of transparent and cost-effective savings products, and poor financial awareness among potential savers. Added to this is the consumerist attitude in South Africa, which often has the ultimate impact of more and more people being highly indebted."

Mr Gordhan also mentions other factors, such as the "persistence of high unemployment, which means people may not be earning enough income to save or might have to use up their savings during lengthy spells out of work."

Steven Nathan, CEO of 10X Investments agrees that these are all factors that drive us to spend rather than save. However he adds, "Why should we expect otherwise when we have laws that enable, even encourage, this poor habit?"

Nathan points out that it is not even compulsory to save for retirement in South Africa. Employers are not compelled to have a work place scheme, and self-employed individuals are not required to set any money aside. Even where employers eventually decide to do the right thing, and start a work place retirement fund, existing employees can still opt out.

In instances when it does become



Pravin Gordhan

compulsory (new hires have to join an existing workplace fund) there is no mandatory minimum contribution. The accepted minimum invested contribution into a retirement fund should be at least 15% of pay.

In South Africa, the average contribution is close to 16%, but the invested contribution rate is only 11.2%, according to the Sanlam *Retirement Survey* conducted in 2009. The balance pays for administration and risk cover.

"That's just not enough," says Nathan. "And even if employees were to save at an acceptable rate, they are not compelled to preserve those savings should they decide to change jobs," he notes.

South Africans love changing jobs – partly for that very reason.

As quoted by Mr Gordhan, 70%-80% of leaving employees don't preserve, according to the Sanlam *Retirement Survey* 2010. It means they can cash-in a part, or even all of their savings, to pay down debt or buy a new car.

Nathan warns that incentivising retrenched staff to access their retirement savings by offering them the same lump sum tax breaks as retiring members is also counter-productive. "Clearly, the difference between old-age retirement and unemployment has not fully crystallised. This incentive merely kicks the can down the street."

Even if investors do decide to preserve at least some of their savings, Nathan notes that they are given yet one more chance to claim it all before retirement.

Which can't come soon enough, as far as Mr Gordhan is concerned - from age 55 in fact.

To make the numbers balance, investors have to save 15% for around 40 years to have a reasonable shot at a comfortable retirement. "In these post-Dickensian times, few of us have a full-time job by age 15," says Nathan. Per-

mitting retirement at age 55 completely disregards rising life expectancies and the prospect that this money may have to last for 25 years or more.

Making matters worse, provident fund investors can elect to take their entire retirement fund as cash. "Most will outlive their capital," says Nathan.

"It would make sense for Government to re-consider the official retirement age," he adds.

Government is looking to make preservation compulsory, and doing away with the 100% cash lump sum option. "That's a good thing," he says. "Even better, retirement saving could soon become compulsory in terms of the proposed social security reform."

Changes also include setting the minimum retirement contribution rate at 10%. Again, a good move according to Nathan, who believes this is only the start. "Perhaps this can be increased to 15% over time, by apportioning pay increases to retirement fund contributions."

But not all the proposed changes support the desired attitude adjustment. By taxing company contributions as a fringe benefit, contributions will, in future, have to come out of the employee's pay. This could very likely turn a fixed rate – set by management – into a discretionary rate, set by the employee.

Further, limiting the total annual deductions to R200 000 may create a savings disincentive for higher income earners. This prevents the late starters in the retirement investment marathon, and those who earn a variable income, from playing 'catch up'.

Nathan warns that it is of even greater concern that it could instil the belief that the annual deduction limit is more than enough. "How exactly does Mr Gordhan reconcile this cap with his desire that 'we need to go beyond what we term 'necessities' in terms of the role of savings?'" asks Nathan. "The retirement reforms are well-meaning, but the message is inconsistent and not entirely convincing."

Returning to Mr Gordhan's original question of 'Why don't we save?', perhaps it's because he makes it so easy for us not to!" concludes Nathan.