Are we grasshoppers or ants?
A retirement fund member's perspective on preservation

Preservation in the South African context

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In a broader context, preservation can be termed as the protection or safeguarding of any asset or natural resource to prevent it from destruction or decay. In the context of a retirement fund, preservation means the act of safeguarding one's benefit in a retirement fund over a long period so as to ensure adequate income after retirement.

In the South African context, the history of preservation is very poor. This is further compounded by the roughly 25% unemployment rate and an informal sector that does not fall within the ambit of any savings pool. Furthermore, within the formal sector there is a general tendency to cash in one's savings whenever the opportunity arises, either through a job change or when experiencing personal financial difficulties. This increases the burden on the state due to more people becoming dependent on social grants. There is thus a great need and responsibility not only on the state but on every individual to try to preserve and increase the saving culture of the nation as a whole.

National Treasury's retirement reform is a step in this direction. The objective of this is to bring more sectors of the population into the realm of a compulsory saving scheme; however, much caution needs to be applied in implementing the reform framework. There needs to be particular emphasis around effective governance, administration, education of members and transparency in the structures. This ensures that the primary objective does not get derailed. Constructive debate and participation within the various interested bodies in the industry need to take place before a final strategy plan is formalised.

International comparison of savings cultures

A recent study indicates that, of those inclined to save, almost 40% believe the safest place to save for retirement is through an employer fund, with 20% opting for investing in property as the safest place for retirement savings.

In the UK, 76% of households with an earning member aged 16 to 64 have pension savings, with the median household retirement savings pot being some £125 000 (R1.9 million at current exchange rates). In general, though, the UK is not deemed to be a nation of savers. In fact, new legislation has been introduced that forces enrolment into an employer retirement fund and is seen as a way to increase the number of people saving towards their retirement. A recent study indicates that, of those inclined to save, almost 40% believe the safest place to save for retirement is through an employer fund, with 20% opting for investing in property as the safest place for retirement savings.

Preservation of retirement savings is compulsory in the UK, where in most cases access to savings isn't possible before the age of 55, with the exception being extraordinary circumstances such as ill-health or early retirement. Enforcement of this rule is strict, with any attempt to access retirement savings early (such as through so-called pension liberation schemes) attracting significant tax penalties, payable by the individual.

Preservation has its own challenges. For example, employees who frequently change employers run the risk of forgetting about small pots of accumulated savings or of failing to maintain contact with the ex-employer. The new Pensions Bill, effective from 2014, introduces measures to ensure ease of transfer of small pots of retirement savings, thereby allowing easier accumulation of funds in one place and removing these risks.

In the USA, only 42% of employees aged 25 to 64 have access to retirement coverage in their current employment. The average of retirement savings is around $40 000 (around R400 000 at current exchange rates) for workers over the age of 50. Preservation is not compulsory, and savers can access their 401(k) savings before age 60 – but they are subject to normal tax rates and a 10% penalty for early withdrawal.

In Australia, contributions to a superannuation fund are compulsory for all employees. This system is largely hailed as a success; however, the latest research shows that accumulated savings are only around A$200 000 for men and closer to A$100 000 for women (R1.8 million for men and R900 000 for women at current exchange rates), which are insufficient to provide a retirement income.

In addition, implementing mandatory savings is not a feasible option for many countries where tensions exist relating to means testing and the perceived disincentive to save.

Rising life expectancy, increased levels of unemployment, slowing growth in assets due to market pressures and the recent financial crises have left retirement planning low on the priority list for a large number of people.

These figures demonstrate that a lack of sufficient retirement savings is not only a South African phenomenon. Rising life expectancy, increased levels of unemployment, slowing growth in assets due to market pressures and the recent financial crises have left retirement planning low on the priority list for a large number of people. In countries where preservation is not compulsory, tough economic times have meant that savers have dipped into their retirement savings to meet short-term needs. Where preservation is compulsory, levels of saving have decreased for the same reason.

A recent study by HSBC highlights the level of the retirement savings problem at an international level. In the UK, it is expected that retirement savings will run out well before halfway through the expected retirement period. The USA is doing slightly better, with savings expected to be sufficient to last two-thirds of the expected retirement period. Even with the success of its mandatory savings approach, Australian retirees are expected to run out of savings just over halfway through their retirement.

Retirement savings shortfall by country

Rank		Length of retirement expected (median, years)	Time when savings are expected to run out (median, years)	Retirement savings shortfall (years)	Retirement savings shortfall (% of retirement covered by savings)
	Global	18	10	8	56%
1	UK	19	7	12	37%
2	Egypt	11	5	6	45%
3	France	19	9	10	47%
4	China	20	10	10	50%
5	Taiwan	18	9	9	50%
6	Brazil	23	12	11	52%
7	Australia	21	11	10	52%
8	Mexico	17	9	8	53%
9	Singapore	17	9	8	53%
10	Canada	19	11	8	58%
11	UAE	15	9	6	60%
12	Hong Kong	17	11	6	65%
13	USA	21	14	7	67%
14	India	15	10	5	67%
15	Malaysia	17	12	5	71%

Source: *HSBC Future of Retirement, A New Reality 2012*

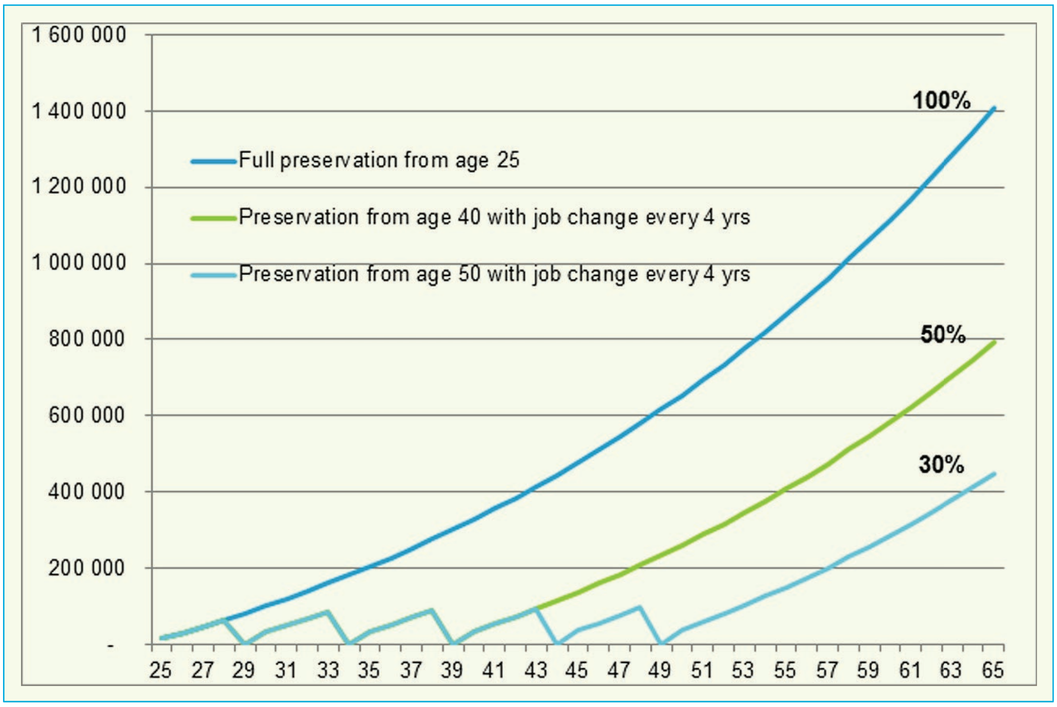
Preservation versus non-preservation

Preservation of retirement savings is an emotive topic in South Africa, where the need for short-term relief from financial distress can be pressing. We have seen a tendency towards a short-term view of saving, even in countries with far lower unemployment rates than that of South Africa. The culture of immediate gratification is widespread globally, with households spending in excess of earnings across the board.

The recent suggested changes to legislation with regard to preservation of retirement funds set out a number of options for how to implement such a change. In theory, it could be argued that accrued rights should not be impacted and should continue to be available to members leaving their current employer. However, the administrative requirements that arise as a result of this approach are significant and need to be considered as part of the process of designing the new preservation legislation.

The argument for compulsory preservation highlights the impact on final savings when withdrawing savings in cash prior to retirement. In the chart below, we can see the impact on savings, in today's terms, of three men who started working at 25 on the same salary. The graph highlights the importance of full preservation from an early age, with a difference of as much as 40% when benefits are not preserved until much later.

The move towards ensuring that a larger proportion of retirement funds be preserved throughout the working lifetime of an individual results in increased security after retirement, but this must be weighed against any genuine need for financial security before retirement.



Assumptions: Working life from 25 to 65

Starting salary of R100 000, male employees

Calculated in today's terms with inflation assumption of 6% per annum, salary inflation at 1% in excess of CPI and investment returns at CPI + 3%

No allowance for expenses

Annual contribution rate 15%

Conclusion

It is evident that some form of retirement reform that encourages preservation is a must for our nation of non-savers.

It is evident that some form of retirement reform that encourages preservation is a must for our nation of non-savers. This has become all the more evident in the current economic scenario. The emphasis needs to be on two main areas in particular:

- Education
- Compulsory forced saving that discourages withdrawal

According to the FSB annual report 2010, there are approximately 12 million people within the ambit of any form of retirement savings in South Africa. This is very low for a nation that has a population of around 55 million people. Another survey recently conducted by one of the benefit administrators found that less than 5% of pensioners were confident about not depleting their savings by the time of their death. This means around 95% of the pensioners are either dependent on, or rely on, social grants. This is a scary picture for all South Africans. If measures are not taken to rectify these statistics and educate the nation on the importance of saving for a rainy day, we will soon become a nation of "grasshoppers*", relying on international bodies to sustain us.

* ***Aesop's fable of the ant and the grasshopper***
A grasshopper spends the warm months singing while the ant works hard to store up food for winter. When winter arrives, the grasshopper finds itself dying of hunger and begs the ant for food.

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