A preservation 'revival' will supercharge South Africa's retirement outcomes

South Africa's retirement outcomes will improve radically if all retirement funding contributions are kept invested when fund members change jobs. Other quick wins include increasing the minimum government pension; delay the government retirement age beyond 60 years; and refocusing the industry from saving a lump sum at retirem to providing a sustainable income in retirement.

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These observations were made by Dr David Knox, the lead author of the Mercer CFA Institute Global Pension Index (GPI) during a keynote address to the inaugural Allan Gray Retirement Benefits Conference.

“An ideal retirement income system should not be solely focused on the provision of a lump sum at retirement; but rather c providing adequate and sustainable income and benefits throughout retirement,” said Knox, as he unpacked the 2020 GPI report.

The GPI ranks the retirement income systems in 39 countries. Overall rankings are based on three sub-category scores fo the adequacy, sustainability and integrity of the system. South Africa, which was 27th out of 39 countries, can learn valua lessons from top performers like Denmark and the Netherlands.

Too much leakage

Adequacy measures the level of income and benefits that citizens receive from a country’s retirement income system at retirement. South Africa performed poorly on this measure due to low minimum pensions; the small proportion of the country’s working age population in formal pension schemes; and too much leakage from retirement savings during workin years.

“The lack of preservation, or our inability to retain retirement contributions within the system, is a long-standing concern fo South Africa,” said Saleem Sonday, head of group savings and investments at Allan Gray, commenting on the report. “However, often the reality is that people access their retirement savings as they have no other option.”

Notwithstanding this, a mindset shift among local savers is needed to change the preservation impasse, to encourage preservation wherever practically possible.

“Government provides a level of taxation support to encourage pension savings; the quid-pro-quo is that this money is specifically for retirement," Knox said.

He further observed that there is a natural tension or trade-off between the adequacy and sustainability measures used in calculating the GPI. South Africa could, for example, improve its adequacy score by doubling the government old age pension; but this would render the country's social security network unsustainable.

Improving performance

Knox touched on four areas that could improve a country's performance on the GPI. First, they should focus on broadenir their retirement system coverage to include the self-employed and workers in the gig economy. Second, they should think about increasing the government pension or retirement age.

"Countries need to manage the system as more of their population lives longer; otherwise they end up with more retirees a fewer workers," said Knox, who emphasised the fine balance between pre- and post-retirement populations. Third, countri must reduce leakage from their retirement funding processes. And fourth, they must reduce fees systemwide, without negatively impacting on retirement outcomes.

Alleviating poverty

Most retirement income systems acknowledge the benefit in scale; but there are risks in driving fees too low. "We must br costs down to lowest sustainable level and take care not to limit retirement funds' access to private equity and infrastructur investment opportunities," said Knox. This is important in a South African context, where the allocation of pension fund ass to infrastructure/impact investment opportunities is a hot topic.

The overarching goals of a retirement income system include alleviating poverty among the aged and enabling retirees to maintain an acceptable standard of living through retirement.

"The Covid-19 pandemic has, more than ever, spotlighted the need for savings, as well as the fact that very few people are prepared to weather the storm in the face of a crisis. The same can be said for retirement; it always seems like something very far in the future, but it is the action we take now that will give us a better chance of achieving the goal of retiring comfortably," he said.