Ignorance about retirement funds problematic, OM survey shows

By Evan Pickworth

9 Oct 2013

Households are looking to external sources such as the government or working children for support after retirement as the economic squeeze continues.

Ignorance about retirement savings is a growing problem too, with about half of the respondents in the Old Mutual Retirement Monitor saying they do not even know how much they have saved and do not know anything about annuity options.

"The concern is that this reliance on future generations only entrenches the cycle of poverty," Old Mutual Corporate's general manager of customer solutions, Craig Aitchison, says.

Karabo Morule, the company's general manager of member solutions, says 39% of the more than 1,180 people surveyed indicated they would like one-on-one or face-to-face communication with their funds. Yet it remains the least offered form of communication by retirement funds, with only 6% of respondents receiving this kind of personal attention. "There is a clear disconnect between retirement funds and their members."

Aitchison says a large portion of the population still has no form of retirement savings in place. The survey found 50% of all respondents list retirement as a specific savings objective, while just under 60% indicated they did not know who their trustees were - an increase from 42% last year.

Trustees must give more advice

Law firm Norton Rose Fulbright's Michelle David, who advises on pensions, insurance and medical schemes law, says unless trustees advise more and "do their duties", a default annuity is something to consider seriously. However, it should not be compulsory, or automatic for all savers, as sophisticated investors will already have preferred savings vehicles.

"There will be some people who have actively considered their portfolios, so as trustees we need to be careful how we treat retirees and treat every one of them individually," David says.

David's preferred model is for those who know no better to be defaulted into a mandatory savings vehicle, but for those who know what they are doing not to be defaulted.

Current proposals are for all employers without funds to enrol their employees in a mandated fund, that allows staff to choose to opt out. Industry and Treasury are busy discussing the levels of the thresholds when individuals must be automatically enrolled in a state fund, who would manage it and how many default funds will be available.

Lower charges required

Research shows that Treasury's move to get South Africa in line with some of the lower charges elsewhere in the world can leave between 50% and 60% more in pension funds. If charges could be cut from 3.5% to 0.5% a year, the same benefit could be received with contributions about half as large. Steven Nathan, 10X Investments' chief executive, is a major proponent of lowering costs below 1% from an industry average of about 3%.

The Treasury's recent paper on retirement cost reform steered clear of naming and shaming the high chargers, or praising the low-cost models, but it can be inferred from the ranking of costs in South Africa that the 10X business model of cutting out brokers and commissions and using diversified index funds, is the low-cost model used on the chart.

Nathan says South Africans are paying too much in fees and it is a myth that actively managed funds will outperform others. He says it is possible to pay less now, not in the future, and get on track to improve pension savings by up to 60% - which a 2% cost saving could achieve.

"You can say you will fly to Mars in the future, but we fly there every day," he says, referring to the industry's ambitions to cut costs, and the reality of low costs on offer at 10X now.

Lack of awareness

The current proposals being discussed and are likely to be legislated next year. They form part of the broader initiative to implement a national social security system, which is likely to take at least another 10 years to implement.

The Old Mutual survey reveals a concerning lack of awareness and education about retirement annuities across all income, age and fund membership levels. A third (33%) of respondents have heard about annuities previously, while 29% have never heard the word "annuity" used in the context of their retirement planning.

"Members often make uninformed decisions upon retirement. This has raised the question of how trustees and other stakeholders can better assist members on retirement - especially when it comes to annuities," says Aitchison.

Despite a preference for inflation-related income among those surveyed, because retirement savings are often inadequate in relation to pre-retirement income, in practice most retirees in South Africa choose the annuity that provides the highest immediate income.

In spite of the apparent lack of knowledge about annuities, just under 80% of respondents said they would feel positive about a default annuity. Only 5% would have no interest in a default option at all. The vast majority would find it useful, even if just as a benchmark. "This is encouraging for Old Mutual, which has advised trustees to provide an annuity default for members," Morule says.

The data also revealed that only 43% of pensioners said they had received pre-retirement advice from their fund or employer.

It also emerged that saving for education remains a high priority among respondents. "Funeral policies continue to enjoy steady support while the incidence of formal retirement products has declined steadily over the past four measures and is at the lowest level to date at 58% of respondents," says Aitchison.