

Retirement savings contributions: Stopping versus reducing, and the impact on your retirement outcome

The nationwide lockdown has resulted in fear and uncertainty. The impact of COVID-19 has shown to be wide-spread, with the need for many individuals looking for options to find some form of financial relief during these difficult times.

Stopping or reducing retirement fund contributions may provide you with immediate financial relief, allowing you to spend the portion of your income that you would usually set aside for your retirement on more immediate needs.

Many individuals have experienced a significant pay-cut as a consequence of the lockdown and restrictions due to COVID-19. Given the uncertainty of the future profitability of many companies, it is expected that reduced pay for these individuals may continue over the short-term, which could be just a few months or even extend to a year.

Liberty Corporate, like many other investment solutions and insurance product providers in the market, have options that help alleviate the financial strain on employers and members of retirement funds during this uncertain period. These include options to temporarily stop or reduce contributions toward your retirement. While these options are available to reduce short-term financial strain, it is also important to remember that you should always aim to meet your retirement goal.

The options are short-term measures, and they are likely to have an impact on your future retirement outcome, as well as a negative impact on the amount of income tax payable.

As an illustration, consider a 40-year old individual who currently has accumulated retirement savings of just over R420 000. When they retire in 25 year's time, at age 65, their total savings is expected to amount to R2,19 million if they continue their current retirement contributions of R1 100 per month. This would allow the individual to purchase an income of R9 130 per month during retirement.

In light of COVID-19, and in order to alleviate financial strain, the individual is considering the following options:

- Stop contributions towards their retirement savings for a period of 12 months,
- Reduce contributions towards their retirement savings by 50%, from R1 100 per month to R550 per month for different periods of time.



What is the potential impact on retirement outcomes if retirement savings contributions are stopped?

Temporarily stopping retirement contributions is likely to be viewed as an attractive option in the current difficult economic environment, as it would immediately increase their take-home pay. However, this is also likely to have a negative impact on their retirement outcome in 25 year's time.

If the individual chooses to stop their contributions for 12 months, and reverts to their original contribution level of R1 100 thereafter, their savings at retirement is expected to reduce to R2,14 million, which would allow the individual to purchase an income of R8 936 per month during retirement. This is a decrease of R50 000 on their savings at retirement, and a decrease of over R2 300 on their yearly income during retirement, compared to if they had not stopped contributing towards retirement for that year.

What is the potential impact on retirement outcomes if retirement savings contributions are reduced?

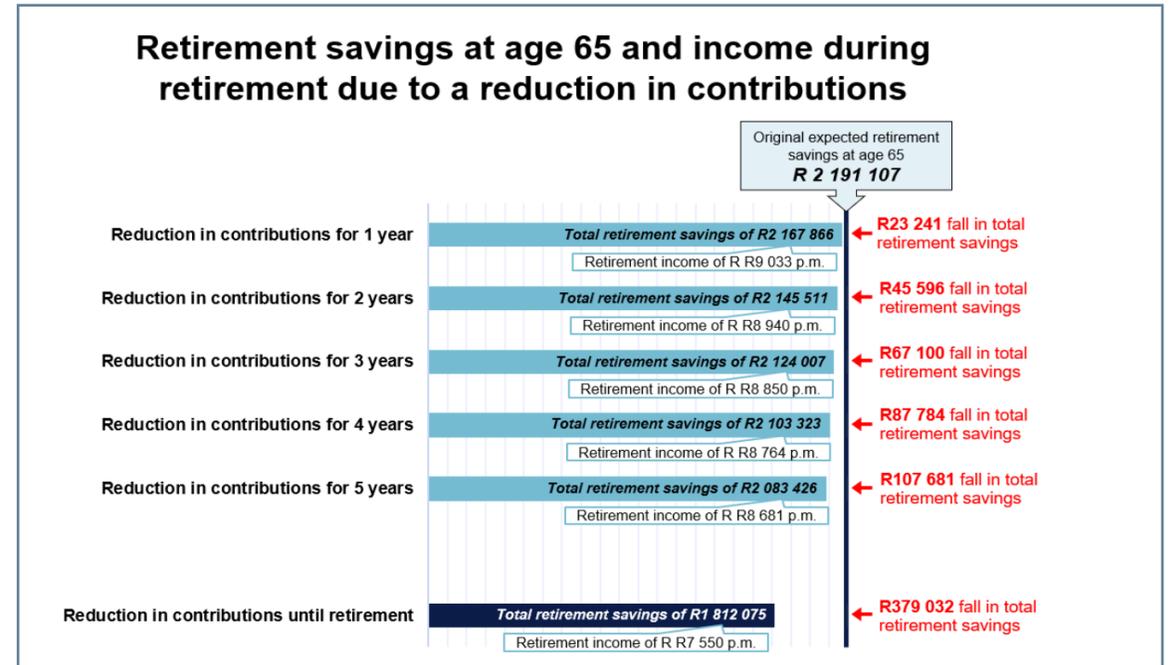
What happens if, instead of stopping contributions altogether, the individual chooses to reduce their level of retirement contributions? This means that while they would benefit from the increased take-home pay, they would also limit the negative impact on their retirement outcome.

To alleviate financial strain, the individual therefore considers decreasing their retirement contributions to half the amount, from R1 100 per month to R550 per month.

If the individual does this for one year, their savings at retirement would amount to R2,17 million, compared to R2,14 million, which is R30 000 more than had they instead *stopped* contributions for one year. This would allow the individual to purchase an income of R9 033 per month during retirement.

Their savings at retirement and income during retirement will continue to reduce if they contribute at this reduced amount of R550 for longer periods of time. Their total savings at retirement is expected to fall by around R20 000 for each additional year of reduced contributions made. This would also result in a reduction in yearly income during retirement of around R1 000 per year, for each additional year of reduced contributions made.

The graph below illustrates the reduction in future retirement savings, as well as income at retirement, for a reduction in contributions made for different lengths of time.



From the above graphic, if the individual continues to contribute only R550 until they retire at age 65, their savings at retirement would amount to only R1,8 million, allowing them to purchase an income of just R7 550 at retirement, over 17% less than if they continued to contribute at the original level of R1 100 per month.

Note: This example is for illustrative purposes only.

Assumptions: The individual is earning R10 000 per month; All projections are shown in today's money terms; All fees are ignored; The prescribed FSCA Living Annuity drawdown rates were used to determine the monthly income after retirement; Gender is assumed to be Female.



How could stopping or reducing your retirement contributions impact the income tax you would be required to pay?

As retirement contributions are tax deductible, stopping or reducing retirement contributions increases your taxable income. This means that you would actually pay more towards income tax compared to if you had made no change to your retirement contribution level.

For example, an individual earning a yearly income of R 200 000, who contributes R20 000 per year towards their retirement would pay a yearly amount of income tax of R 17 442. If this individual halves their retirement contribution level, to R10 000 per year, their yearly income tax would increase to R 19 242. If, instead, the individual stops contributions for that year, they would pay R 21 042 in income tax, which is 20% more than they would have paid if no change was made to their level of retirement contributions.

Stopping or reducing contributions may increase your take-home pay, however, it increases the amount of income tax you are required to pay and should therefore be considered before making these types of decisions.

The key message

While you may need to make short-term adjustments to your retirement savings contributions due to the impact of COVID-19, doing so for long periods of time should be cautioned against. You could be better off in retirement if you reduce, rather than stop your retirement fund contributions for 12 months.

A temporary stop to contributions may not be detrimental to your retirement outlook. However, if you choose to keep your retirement contributions at a reduced level for a long period of time, it could impact your retirement outcome significantly.

It is important to remember your long-term retirement goal, and ensure that once the impact of COVID-19 eases, you revisit the level of your future retirement contributions so that your retirement goal can still be met.



Professional assistance and emergency services to help you in the time of COVID19

As we enter the 7th week of lockdown it may be harder to stay indoors and, possibly, away from loved ones, but we continue to do so to adhere to our government's regulations and thereby saving lives. We are in a period of uncertainty which may manifest into worry about our health, the health of our loved ones, concerns over the economy, potential job losses and the ability to provide for our families. This could lead to increased stress and anxiety and may require the need to speak to a professional.

An online survey conducted by the South African Depression and Anxiety Group (SADAG) reveals that 65% of the respondents felt that they were stressed or very stressed during the lockdown. The survey was conducted across gender, age, race and socio-economic background which highlights that mental illness does not discriminate. Many of the survey respondents indicated that they were suffering from anxiety and panic, financial stress and pressure, as well as depression. SADAG has also reported that they have received an increased number of calls for support since the start of the lockdown.¹

As Liberty, we want to remind you that we are in it with you. Liberty Corporate has partnered with Cims South Africa (Pty) Ltd (Cims) to provide value-added services at times when you need it most. These services include:

- [Trauma Helpline;](#)
- [Medical Information and Advice;](#)
- [R5 000 for Hospital Admission Guarantee;](#)
- [Emergency Ambulance Assistance; and](#)
- [Legal Advice Helpline.](#)

Cims has reported a significant increase in the number of calls from our Liberty Corporate clients requesting support relating to trauma counseling and legal advice since the start of the lockdown.

All the services mentioned above are available to you as a Liberty Corporate client as well as your spouse and child dependents under the age of 21. To qualify for the services, your employer must simply have a Liberty Corporate risk policy or be part of the Corporate Selection suite of Umbrella Funds. If your employer has taken a funeral policy with us on your behalf, you and the insured lives under the policy will have access to funeral assistance services, including body repatriation.

To access these services which are available 24-hours a day, please call the numbers below:

[South Africa](#) 0861 724 247

[International](#) +27 11 966 5011

¹http://www.sadag.org/images/newsletter/SADAG-Making-Mental-Health-Matter-during-COVID19_compressed.pdf