

Navigating through the current economic environment when making decisions in the event of retirement, resignation or retrenchment

The national lockdown continues to impact many organisations in South Africa. As a result, some employers are now considering reducing the size of their workforce to help alleviate the consequent financial strain on their businesses.

On 30 April 2020, the National Treasury released a brief on the financial implications of COVID-19 on both the economy and the budget, stating that at least 3 million people are expected to be at risk of retrenchment. This is a significant portion of South Africa's total workforce, which was just over 10 million in December 2019, as reported by Statistics South Africa.

If you, as an employee and member of a retirement fund, are affected by retrenchment, resignation from your current job or nearing retirement, it is important to understand and consider all options available to you before making financial decisions, to ensure that you can still meet your retirement goals as best as possible in the current economic environment.



What are your options if you resign or are retrenched?

If you resign or are retrenched, you would typically have the option to keep your accumulated retirement savings in your current retirement fund, move it to a preservation fund or withdraw it as cash.

While having additional cash may be attractive during times of uncertainty, it is important to understand the consequences of cashing out your retirement savings before retirement. One of the consequences is that the cash withdrawn from your retirement savings will be subject to income tax. This means that if you choose to withdraw all of your retirement savings in cash, the amount you would actually receive in your bank account would be less than the amount that you have accumulated. This, however, is not the case for cash withdrawals of R25 000 or less, as the once-off tax-free withdrawal threshold would apply.

In making the decision to withdraw cash from retirement savings prior to retirement, the short-term benefit of having cash at hand today should be weighed up against the long-term impact of effectively saving less towards your long-term retirement goal in the future.

Alternative options are available that enable you to preserve your retirement savings, either by keeping your savings invested in the retirement fund which you are currently a member of, or investing your accumulated retirement savings in another preservation fund. In these instances, there are no tax implications on your retirement savings that are preserved, which means that you are likely to have more money at retirement compared to if you had instead cashed out your retirement savings. Members who choose to preserve their retirement savings also have the option of withdrawing their preserved money before retirement.

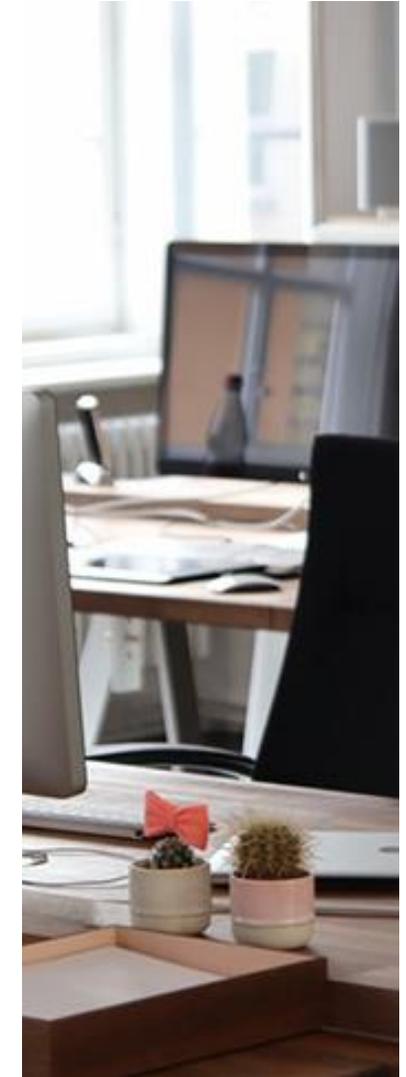
Withdrawing cash prior to retirement may be helpful if your financial situation changes and you need access to cash, however, this option should be used with caution as it may negatively impact your retirement goal and the ability to have enough money to live a comfortable retirement.

Consider a 30-year-old individual who has accumulated R154 800 in retirement savings. When they retire in 35 years, at age 65, their total savings is expected to amount to R2,19 million if they continue contributing at their current retirement contribution rate. This would allow the individual to purchase an income of R9 120 per month during retirement. The individual has just resigned from their current job, and has chosen to withdraw all of their retirement savings in cash. Just after this, they start a new job and contribute towards their retirement at the same contribution rate as previously. Their savings at retirement is expected to reduce from R2,19 million to R1,21 million, which would allow the individual to purchase an income of R5 040 per month during retirement. This is a decrease of almost R1 million on their savings at retirement, and a decrease of over R4 000 on their monthly income during retirement, compared to if they had preserved their retirement savings.

The impact on one's retirement outlook when withdrawing all accumulated retirement savings prior to retirement is greater for older individuals, compared to younger individuals, as they have less time left during their working life to save towards retirement.

To illustrate this point, consider a 50-year-old individual who is contributing at the same rate and is expected to have the same total savings at retirement as in the example above. This individual also resigns from their current job and has also decided to cash out all of their retirement savings, which amounts to R878 220. This individual then starts a new job, and contributes towards their retirement at the same contribution rate as previously. Their savings at retirement is expected to reduce from R2,19 million to just R271 050, which would allow the individual to purchase an expected income of R1 130 per month during retirement. This is a decrease of more than R8 000 on their expected monthly income in retirement which they would have received if they had not made the cash withdrawal, which is almost double the decrease compared to if this had happened when they were 30 years old.

Assumptions: The individual is female. The individual starts contributing towards their retirement at age 20, and receives a starting salary of R100 000 p.a. All fees are ignored. The current prescribed draft FSCA Living Annuity drawdown rates are used to determine the monthly income after retirement. All projections are shown in today's money terms.



What are your options if you are retiring?

Many individual's investments have been impacted due to the effects of COVID-19 on underlying assets and financial markets all over the world. If you are an individual retiring during this time, the impact of COVID-19 may have caused a significant amount of uncertainty about your retirement outlook.

However, annuity options are available to meet your needs in all economic environments, including the current one. An annuity provides a member with a regular income in retirement. The two main types of annuities available in the market are guaranteed annuities and living annuities.

What is a Guaranteed Annuity?

This annuity provides you with an income for the duration of your remaining life as well as a choice of how your income would increase in future years. For example, you may choose a level annuity where your income remains the same throughout your retirement.

Alternatively, you may choose an increasing annuity where your increases can be a fixed percentage, CPI-linked, or driven by the performance of an investment portfolio.

The starting income for a guaranteed annuity is currently higher than it was prior to the COVID-19 pandemic, due to higher bond yields. Members of the Liberty Corporate Selection suite of Umbrella Funds could purchase a guaranteed annuity, called Growth Pension (2018), which would allow them to obtain increases linked to market returns.

This means that you are guaranteed to receive a monthly income that will not decrease in Rand terms, whilst benefitting from potential future market growth in terms of future increases that target inflation.

What is a Living Annuity?

A living annuity allows you to manage your investment portfolio choices and choose the income level that you want to receive each year. Your income is not guaranteed and would depend on the performance of your investments.

Therefore, regular monitoring is required to ensure that you don't run out of money during your lifetime. Unlike guaranteed annuities where all payments usually stop once you pass on, a living annuity provides the advantage of having the balance of your investments paid to your beneficiaries.

It is likely that your retirement savings have decreased in line with the market decline caused by COVID-19. Investing in a living annuity in the current market environment, however, provides the advantage for members to participate in any potential future market recovery.



The impact of fees on your retirement savings

When saving towards retirement, and when thinking about underlying investments or investment portfolios, market performance and investment returns are often first to come to mind. However, fees also have a significant impact on retirement savings and retirement outcomes.

A paper by National Treasury titled Charges in South African retirement funds published in July 2013 has found that an individual who reduces their retirement savings investment fees from 2.5% of their yearly investment to 0.5% of their yearly investment would receive 60% more money in retirement after 40 years, all else being equal.

In deciding on the best option on what to do with your retirement savings in the event of retrenchment, resignation or retirement, the associated fees for each option should also be considered.

Liberty Corporate offers institutional pricing for our preservation and annuity solutions for all of our members. This means that members benefit from the cost of the managing of the fund being shared amongst a larger group of individuals, through their employer. In most cases, these fees are less than an individual would pay when preserving their savings or purchasing an annuity in their personal capacity.

Support during retrenchment or retirement

Retrenchment and retirement can be an overwhelming experience. Liberty Corporate provides benefits counselling services to aid in educating you and providing you with information regarding the preservation and annuity options available to you which can enable more informed decisions.

These services are available in multiple languages and are at no additional charge with clear, easy to understand information and explanations regarding investment portfolios and risks, costs and charges. You may contact our benefits counselling team by calling 011 558 2999 or emailing benefitcounselling@liberty.co.za.

It is important to note that benefits counselling is a legislative requirement and does not entail the provision of financial advice. Professional advice should be obtained from your financial adviser when making all financial decisions or planning for retirement.

Deciding what to do with retirement savings is an important decision and many factors such as risk appetite, personal preferences, time horizon and retirement goals should be considered. This is no different in the current COVID-19 environment and a financial adviser can assist in finding the correct product for you.



Risk benefit options in a time of COVID-19

The COVID-19 pandemic has brought about significant uncertainty for individuals and their families, as well as economies and governments all over the world. Many employers have not been able to operate at all or at optimal levels which has led to severe financial pressures. With many of the lockdown measures still firmly in place in South Africa, this is expected to continue for the foreseeable future. Some employers may have no choice but to reduce their workforce to relieve some of the financial strain. If you find yourself in the unfortunate position of being retrenched or dismissed, this would translate into no longer being part of your employer's retirement fund and losing the group risk benefit cover your employer had purchased for you on your behalf.

The continuation option offering

A continuation option entitles you to apply to retain your insured risk cover through an individual policy within 60 days of leaving your employer's retirement fund. If the continuation option is selected as part of your benefit offering by your employer, you may obtain certain risk products available in the group risk scheme that have a corresponding risk benefit offering on an individual basis which are available at the time of applying for these benefits. The option will not require you to produce any evidence of health to Liberty. However, cotinine tests may be required to confirm smoker status. In this way, you may continue your valuable insurance cover, at your own expense, subject to restrictions and limitations as provided for in the relevant individual policy.

The continuation option is available on withdrawal from your group risk scheme, which includes resignation, retrenchment and dismissal as well as retirement that is not related to ill health. A list of the individual policies that correspond to your risk benefits can be obtained through your financial adviser or our benefits counselling team.

If the continuation option is available to you through your employer, exercising it may benefit you by allowing you to obtain similar risk cover on an individual basis without having to provide evidence of health. However, the option will not be available to some individuals depending on their circumstances and state of health. For example, if you have been a member on a group scheme for less than 12 months, or have previously received a partial of full dread disease payment, this option will not be available to you.

Additional support in the form of value-added services

The COVID-19 pandemic brings with it added uncertainty of future job prospects, and therefore, the ability to provide for our families. This may lead to increased stress and anxiety and may require the need to speak to a professional.

As Liberty, we want to remind you that we are in it with you. Liberty Corporate has partnered with Cims South Africa (Pty) Ltd to provide value-added services at times when you need it most. These services include a trauma helpline and a legal advice helpline that is available to counsel and advise you should you be retrenched or dismissed.

These services 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.

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

South Africa 0861 724 247

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