Press release
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JUST.

RETHINK RETIREMENT

WHAT RETIREES WANT VS WHAT THEY ARE SOLD

By Justine Wyatt, Legal and Compliance Executive at Just Retirement South Africa

In a recent survey conducted by specialist annuity provider Just Retirement South Africa, retirees stated a clear preference for income security in retirement, with no financial risk. However, when it comes to investing their retirement savings they act completely contrary to this.

A total of 86 percent of responders said they prefer to receive a guaranteed income for life as opposed to investing their retirement savings and deciding how much to draw each year but running the risk of depleting their savings during retirement. The survey involved interviewing a cross section of people between age 55 and 70 in Gauteng, Cape Town and Durban.

Surveys of over 5,000 individuals carried out in Australia found that the majority of people prefer a stable income for life, rather than taking risks in managing a pool of assets and choosing how much income to draw. Results from one Australian survey* suggest that more than 90 percent of Australians over age 50 believe that “money that lasts my lifetime” is very important. The reasons why 89 percent of South Africans choose living annuities are due to market inefficiencies and not due to people’s preferences. These market inefficiencies are well documented in the National Treasury paper, ‘Enabling a better income in retirement’.

Half of the responders in the Just Retirement survey disagreed with the statement: “I do not mind taking risks with my money for saving or investment purposes.” Almost 44 percent said they could not afford to lose any of their retirement savings before it would seriously impact their retirement plans.

Most responders also said that retirement income for their own needs is more important than providing death benefits for dependants or beneficiaries.

In spite of retirees’ needs and preferences, 90% of retirees purchase living annuities at retirement. Unlike conventional guaranteed annuities, living annuities require retirees to choose how they invest their retirement savings, which subjects them to market risk. Retirees are also exposed to longevity risk, which may see them outlive their capital. Living annuities were not developed to provide for the needs of all retirees.

Determining an appropriate target market for a product, and offering that product to that specific target market, are clear requirements of the Treating Customers Fairly (TCF) principles and it should be incumbent on all product providers to embed these principles into their corporate culture. It is difficult to see how offering ‘one-size-fits-all’ living annuity solutions to the majority of retirees fits with a TCF culture.

It is important that retirees seek a clear statement from the product provider and their adviser about which target market a product has been designed for and why it is appropriate for their specific needs. Many retirees may find that an enhanced annuity, with-profit annuity or other conventional/guaranteed annuity is a far better choice to meet their preference for a no-risk, guaranteed income for life.

Another reason National Treasury has highlighted for retirees purchasing living annuities relates to remuneration distortion. Financial advisers receive significantly more remuneration for selling a living annuity than a guaranteed annuity. In addition, legislation makes it unattractive for advisers to transfer their clients from living annuities to guaranteed annuities should their circumstances change over time. It is unfortunate that regulation introduces a conflict of interest into the advice process and Just Retirement is a strong advocate for equivalent remuneration for guaranteed annuities and living annuities up to an income level that supports basic living expenses.

It is also unfortunate that consumer protection in SA is not as rigorous as in some other countries. In South Africa, compliance officers check that a record of advice exists, but the actual quality of the advice is not scrutinised. Quality is only assessed if a complaint is made to the Ombud, and this is far too late in the process for retirees to benefit.

In the UK, the UK Financial Conduct Authority requires providers of annuity products to issue risk warnings to potential clients to ensure they have considered all relevant factors when choosing a product to provide retirement income. For example, the Association of British Insurers' Code of Conduct on Retirement Choices requires that conventional guaranteed annuity providers make the following statement during the sales process: "We do not offer a rate based on your health or factors that affect how long you might live, such as medication you take, where you live, your occupation and whether you smoke. This is known as an enhanced annuity and if you are eligible for this type of annuity, another provider could offer you a much higher level of income." In addition, the UK Regulator conducts mis-selling reviews to ensure that appropriate advice is given to clients.

Another reason for the popularity of living annuities is the fact that the product is seen to provide death benefits as any capital remaining in a living annuity at a retiree's death can be paid to their beneficiaries. It is argued that retirees want this benefit. However, Just Retirement's research and the finding of the National Treasury in its retirement reform papers do not support this contention. It also does not make sense when, according to the 2015 Sanlam Benchmark Survey, 94% of retirees do not have sufficient savings to support themselves in retirement. In this context, retirees who opt for a living annuity will in all probability never receive any death benefit but rather they will become dependent on their children or the state when their money runs out before they die.

The research results illustrate a significant gap between what retirees are expressing as their financial needs and the products they end up with. This is due to a combination of regulation introducing conflicts of interest, product providers failing to state clearly the specific target market for which they have designed the products, and insufficient consumer protection. Just Retirement has earned a reputation in the UK of championing improved consumer outcomes in the face of vested interests and is intent on highlighting issues in South Africa and actively working to address these through product innovation.

* December 2013 Retirement Income Report, Investment Trends, Sydney. Based on a survey of 5,730 Australians aged 40 and older (as quoted on Page 120 of Murray Financial System Inquiry, released 7 December 2014). http://fsi.gov.au/publications/final-report/

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