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BUDGET REVIEW – WHY ARE RETIREES SO BADLY OFF?

The 2018 budget will place increased pressure on retirees' disposable income because of income tax bracket creep. Simply put, inflationary annuity income increases may have pushed some middle to high income earners into a higher tax bracket.

Against this background, the tax relief available on retirement savings becomes ever more important.

Linked to the income tax brackets are the primary, secondary (for people aged 65 to 74) and tertiary (for people of 75 and older) rebates that have been subject to below-inflation adjustments: 3.17%, 3.8% and 3.25% respectively.

"Once an individual reaches retirement, how effectively they use their retirement savings is as important as taking advantage of the tax rebates. It is concerning that taxes are increasing with below inflation rebates putting more pressure on the retiree who may or may not have had an inflationary adjusted increase in their annuity income," warns Justine Wyatt, Legal and Compliance Executive at Just.

Financial pressure in retirement is compounded by retirees drawing down too much income to sustain their assets in retirement and failing to invest their retirement savings appropriately.

Recent amendments to the Pension Funds Act require trustees of retirement funds to provide appropriate retirement strategies to retirees upon their retirement to try and ensure that their savings pay an income for the rest of the retiree's lifetime, eliminating the risk of outliving their assets.

"However, many trustees are establishing default annuity strategies which inadvertently set up their members for failure by giving them little to no guidance about the sustainability of their income in retirement and by not providing an option to secure a guaranteed income for life," says Wyatt.

A key risk is a retiree outliving their assets in retirement and seeing income fall dramatically in the final years of their life. Wyatt adds that very few retirees are able to assess this longevity risk for themselves. In fact, data shows the average drawdown rate from living annuities is 6,6% which is above the sustainable drawdown rate recommended by the Association of Savings and Investments South Africa (ASISA) – and to make matters worse, this average is skewed by the fact that some people with large retirement savings pots draw very little.

By extrapolation, this means that the majority of living annuitants are drawing income at an unsustainable level that could see them becoming dependent on their families or the State later on.

Another mistake that retirees make is not growing their portfolio after retirement.Taking too little investment risk may contribute to retirees being worse off. A portfolio has to consistently perform in excess of 10% to ensure that a retiree does not outlive their assets. Ideally they would want to cover their basic living expenses so that they can grow the remainder of the capital.

“The solution is an asset class available within a living annuity which allows an individual to draw a higher level of income than recommended by ASISA, for this income to be guaranteed for life, and for the income to be targeted to grow with inflation. This allows a retiree to invest their remaining assets within the living annuity for long term growth.

“Just provides income solutions that improve the lives of retirees and meet their needs while addressing key concerns raised by Treasury in recent years. Our focus is on giving retired South Africans financial certainty and helping them achieve a secure retirement,” concludes Wyatt.

For more information or to set up an interview, please contact:

Lisette Lombard
Firefly PR
Independent Communications Consultants
Tel: +27 (0)82 836 8036
Email: info@fireflypr.co.za