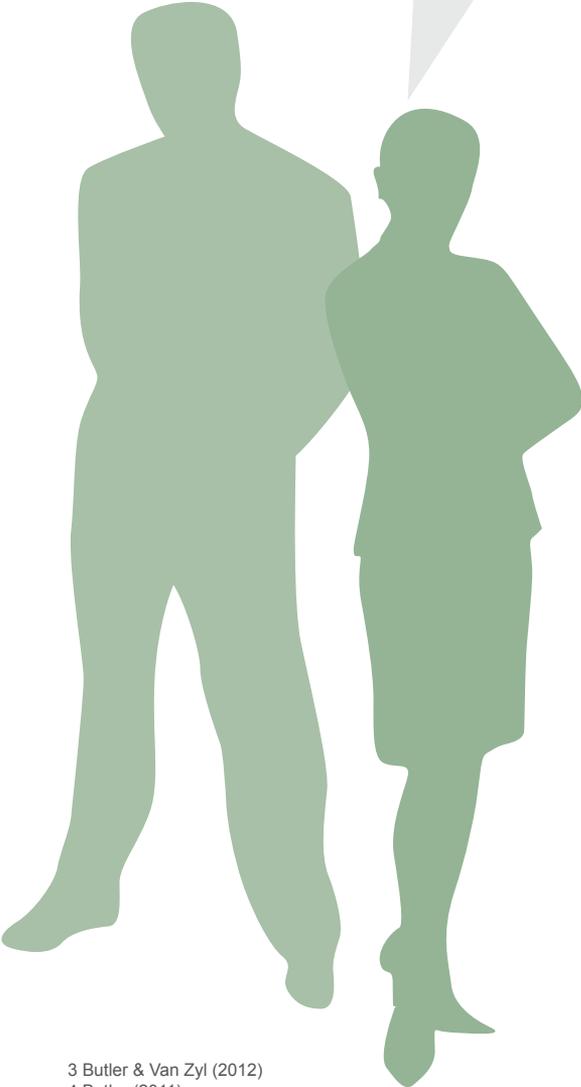

WHAT MAKES A TARGET MEANINGFUL?

In setting a target at fund level, there are a few desirable characteristics that the target must fulfil, like:

- Targets must be:
- 1. Realistic
 - 2. Communicable
 - 3. Balanced against other needs
 - 4. Based on income requirements



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1 THE TARGET IS REALISTIC

Trustees cannot set targets independently of the current design of the retirement fund. Contribution rates, expenses, normal retirement age and other pertinent factors are required to project the possible retirement funding outcomes that members could achieve. Sensitivity testing under a range of investment return assumptions can help to provide the range that the target must fall into. If members' projected outcomes are clearly inadequate, an exercise of this sort may also provide an indication that trustees may need to redesign the fund.

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2 THE TARGET IS COMMUNICABLE

Short service periods indicate that members may be accumulating their retirement funding from a number of different sources. As a result, it may make sense to communicate goals in terms of multiples of salary given that these are mathematically simpler to manipulate than replacement ratios³. This is the wealth-earnings ratio we describe later. Current estimates suggest that 75% of single men need 12.9 times annual salary at age 65⁴. The comparative replacement ratio is 90.9%⁵. We argue later on in this chapter that trustees may find a goal that reflects a multiple of a member's annual salary far easier to communicate to their membership.

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3 Butler & Van Zyl (2012)
4 Butler (2011)
5 Butler (2011)



Members may have to address **potential shortfalls** between fund targets and their unique targets.

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3 TARGETS ARE SET SUCH THAT THEY BALANCE OTHER NEEDS

In an effort to maximise their retirement funding outcome, individuals face conflicting objectives. They can increase their savings rate, but they will have to sacrifice take-home pay. They can allocate the highest possible portion of their retirement fund contributions to the investment vehicle, but that would be at the expense of important protections of their income and families. Setting a target realistically would involve finding that balance and looking at the problem holistically.

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4 THE TARGET IS BASED ON EXPECTED OR ASSUMED INCOME REQUIREMENTS

Individuals will have variable views on how to spend their retirement savings. Some may choose an inflation-linked income while others may choose a fixed, guaranteed income for life. We may need to change the way we calculate the target to accommodate these differences. For instance, if members all intend to buy an inflation-linked income, then we should calculate the replacement ratio based on inflation-linked annuity rates rather than a fixed, guaranteed annuity.

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Perhaps the most practical suggestion is for trustees of DC funds to have a goal that includes both the total amount an individual needs to save, as well as some broad indication of what their savings will translate into at retirement to provide that post-retirement income. The goal may not, however, fulfil all of a member's income requirements and trustee boards should communicate this to members. Armed with that information, members can then at least determine for themselves what their total picture is likely to be and whether they need to find alternative ways to address potential shortfall issues.