The Bigger Picture on improving employee engagement with benefits

What's the context? The role of culture

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Culture cannot be ignored

Case study/Lesson

In South Africa, it is not only the private and public sectors that play pivotal roles in social protection, it is also families and communities. This is typical in both emerging markets and African countries, but plays a far more muted role in developed markets.

According to the World Economic Forum's latest Global Competitiveness Report, South Africa has the world's third most developed financial market[1]. While this is an accomplishment, it also raises significant risks for the country because what we may end up doing is imposing a developed world model of savings behaviour onto an emerging market, where a large contingent of the population uses collective savings structures.

In addition to being an emerging market, South Africa is challenged by inequality, which means a single approach to savings and insurance is even less likely to apply to all. Different segments of income earners may use different mechanisms for savings and protection. This has implications for social protection, and employee benefits in particular. Not everyone has the same goals and priorities.

To make the social protection system work, we need to understand how South Africans solve financial problems in practice. The culture of South Africans influences the choice of financial products that they take up, but it also constrains their ability to participate in some formal arrangements into which policy makers and employers may be pushing them.

A spending culture?

In their report titled 4 Million and Rising, the Unilever Institute of Strategic Marketing found that the black middle class population in South Africa has grown rapidly over a period of eight years, from around 1.7 million people in 2004 to around 4 million people in 2012. The black middle class is characterised more by the fact that they are driving better cars and using more technology than by where they live[2]. Collectively, this population has a spending power of around R400 billion a year[3].

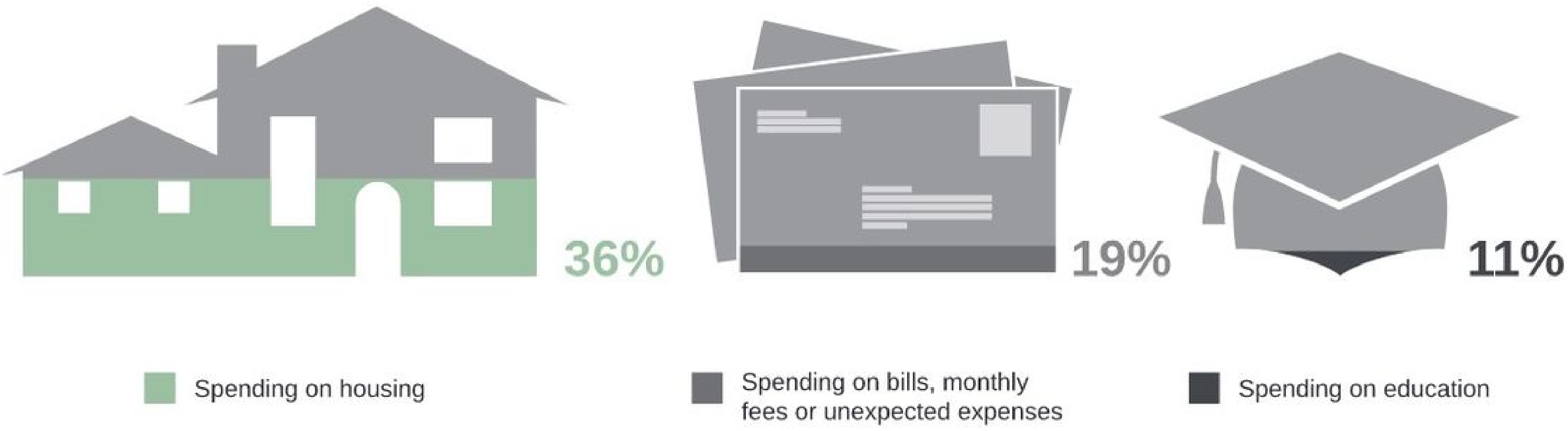
The South African Reserve Bank reports that the ratio of household debt to disposable income at the end of 2013 stood at just over 74%, a figure which most economists would consider high. Given the legacy of our country, should we be worried?

During Apartheid, many millions of black South Africans were denied access to formal investment and credit products[4]. Once such bans were lifted, the number of new loan recipients surged. Many were accessing longer-term loans to finance houses since there was an enormous pent-up demand for housing after the 1994 elections. By 2012, around 65% of the black middle-class population in South Africa owned their own homes[6].

Often, concerns are highest around unsecured debt, but the latest Finscope numbers[7] show that 36% is spent on housing and another 11% on education, with only 19% spent on bills, monthly fees or unexpected expenses.

The high debt ratios we are seeing may be a result of the increase in lending following the lifting of Apartheid restrictions. As people pay off these loans, we may well see a decline in the debt to disposable income ratio.

SOUTH AFRICAN DEBT PATTERNS



Source: Finmark Trust (2013)

> **Evidence suggests that South Africans do save, but it may not be in the way other stakeholders want or expect.**

A savings culture?

Conventional aggregate measures of savings would lead us to conclude that South Africans do not save. Perhaps we need a broader definition of this concept to understand the dynamics at play. Evidence suggests that South Africans do save, but their ways of doing so, and their priorities, may not be what other stakeholders want or expect. As a result, their savings may not be formally measured.

Stokvels – a multi-million rand industry

It is widely known that there is an informal savings sector in our country which caters to approximately 33% of the population[8]. Previously conceived notions about the lack of saving among low-income earners have been refuted with evidence from the Finmark Trust, which showed that 48% of individuals in LSM 5–6 who have an average monthly income of R4 497.60, are using stokvels for short- and medium-term savings.

A stokvel is a group savings scheme providing for the mutual financial well-being of participants, as well as social and entertainment needs[9]. Individuals within the same community or family voluntarily make contributions on a regular basis which are used for an agreed purpose. Each member of the group has access to the funds whenever a need for it arises, as long as they keep up to date with their contributions. Despite being classified as a type of informal savings vehicle, stokvels are relatively formally structured in their approach. They are governed by a constitution[10] and it is not uncommon for stokvels to elect a treasurer[11]. Most stokvels will deposit their contributions into bank accounts[12].

This illustrates how many South Africans solve their financial problems via collective, rather than individualised, mechanisms.

Alternatives to retirement savings

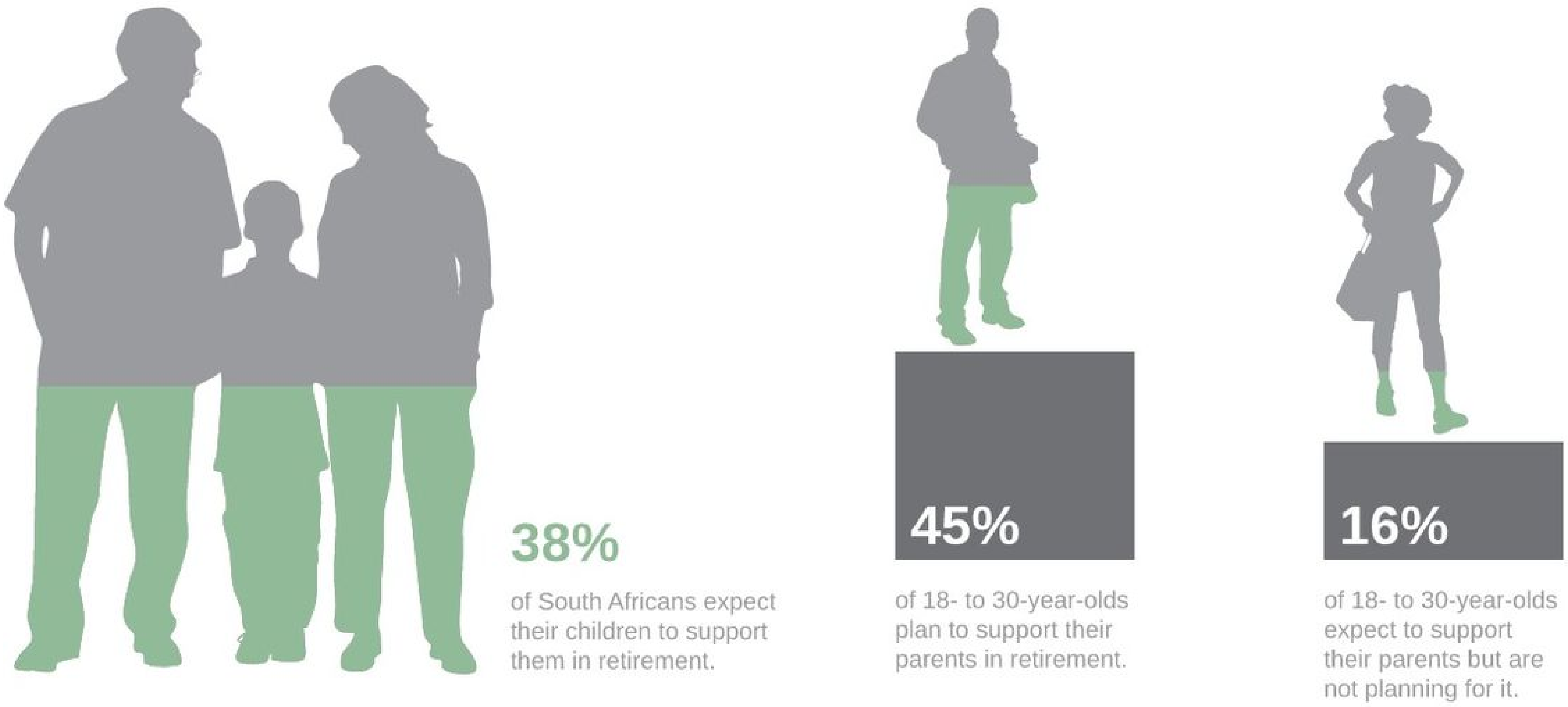
The financial services industry often places greater emphasis on retirement outcomes and having sufficient savings and insurance for emergencies. However, as we raised in Benefits Barometer 2013[13], individuals often have other financial priorities.

What is particularly significant with housing and education is that both act as partial substitutes for retirement savings and other forms of social protection. In the case of education, the World Bank recognises that:

"If in a particular context there is a well-established tradition according to which adult children support their parents in their old age, it may make perfect sense for a person to use her savings to finance her children's education rather than investing it in financial products[14]".

In South Africa, the Old Mutual Savings and Investment Monitor consistently reports that a large proportion of South Africans expect to be supported by their children in retirement – the latest figure from July 2013 being 38%. In the same survey, they found that 45% of 18- to 30-year-olds are planning to support their parents when they are old, with another 16% expecting it, but not planning for it. This is normally seen as negative because it indicates dependency, but given the World Bank's comment, it doesn't have to be. Concerns around dependency on family are typical of a Western mindset which focuses on independence, but may not be relevant in cultural contexts with higher levels of social capital.

Financial support in retirement

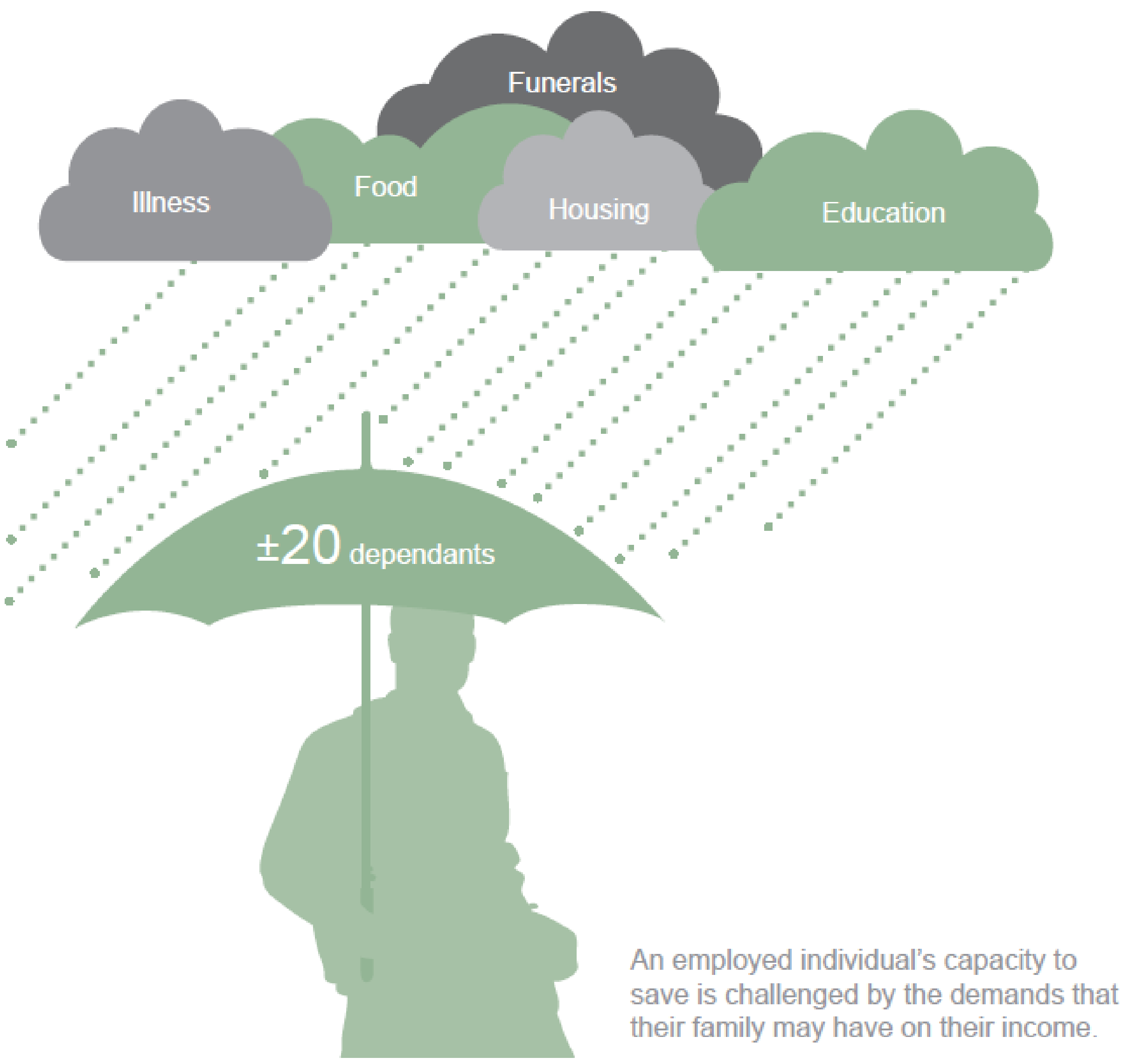


Source: Old Mutual (2013)

Furthermore, even among the South African poor, a child's education is often seen as a key avenue for escaping poverty, with tertiary education being one of the primary reasons for long-term savings among this group[15].

In the case of housing, the Organisation for Economic Co-operation and Development's work shows that owning a house in retirement often reduces the incidence and severity of old-age poverty[16]. Housing is not only an asset; it can also provide an income, or relieve the amount of income an individual needs. According to the latest Income and Expenditure Survey, imputed rent accounts for 20.5% of the average household's expenditure – this is an estimate of the rent an owner would need to pay to occupy (or rent) an equivalent home. This suggests that owning a house, particularly when it is mortgage-free, can account for a significant reduction in the amount of income required at retirement. While the government is working to address education and housing, these interventions are aimed at the poorest and don't represent a comprehensive solution for all. For households aspiring to a higher standard of living, they need effective mechanisms that facilitate their full set of priorities.

The choice: Saving or taking care of dependants?



An insurance culture?

Shocks are particularly detrimental to the poor, as they have few resources left to absorb these shocks[17]. Medical emergencies, funerals and crime are the key shocks that can set the poor back[18]. In preparing for these shocks, the poor may have some access to formal products – for instance, if they work in the formal sector, they may have funeral cover through their employer. But the poor often use social ties to manage risk and vulnerability[19].

This is particularly important given the complexity of South African households. A working household earning under R60 000 per person per year may well support two or three others outside their household. In extreme cases, a worker can have more than twenty dependants, including their own household.

Often a household like this ends up with a 'stationary demographic structure' in which old people, as they die, are replaced by a new generation of old people, while young people at the bottom of the range shift up to make way for children[20]. A household then internalises many of the insurance activities which would require saving or formal insurance. Further, the close relationships between the individuals concerned may also mean that the quality and sustainability of the protection is high.

This has significant implications for the employed members of a household or community. Individuals who have stable employment are obliged to give back to their family or those who raised and supported them. They might be required to cover the cost of housing, food, healthcare and education for younger siblings, while balancing their own cost of living.

Furthermore, consider the impact of having a funeral for a family member: funerals can cost up to R50 000 and the burden of covering the cost of a funeral often falls to the employed members of the family. This cost may not relate to immediate family only, but to the extended family as well.

Realising how important this can be to employees, many employers offer funeral benefits, even though they are an unapproved benefit for tax purposes. But to provide a benefit that is considered truly valuable in a typical South African household, employers need to consider funeral insurance that covers the death of a member of the extended family of the policyholder.

As a result of all these wealth transfers, employed individuals are often left with little disposable cash for voluntary savings. On the one hand, compulsory fund membership of an occupational retirement fund may ensure these individuals do not end up without any resources in retirement. On the other hand, their capacity to save is challenged by the demands that their family may have on their income.

> **As a result of being financially responsible for extended families, employed individuals are often left with little disposable cash for voluntary savings.**

Conclusion

We decry the shabby state of savings in South Africa. We marvel at the levels of underinsurance of the households who have employed family members. But is this really the whole truth?

What we have argued here is that how South Africans spend, save and insure is much more complicated than macro-figures make us think. And we need to engage with that. We need to engage with the reality of our country and design our social protection and employee benefits accordingly.

While policymakers are currently focused on trying to improve long-term savings, they should be more cognisant of the relative importance of long-term savings in the lives of ordinary South Africans. Mortality estimates show that around half of South Africans currently aged 15 will make it to retirement age[21]; informal conversations with ordinary South Africans indicate that many believe they will not make it. These people may not see the value in sacrificing current consumption for a future that may not materialise.

That's why in The way forward to improving employee benefit engagement: We argue that we have to engage with an individual's entire journey and all the trade-offs along the way. One of the great ironies of the financial services industry is its tendency to focus on those who need its assistance the least. It is the groups that face real trade-offs that most require the minds of the financial services industry to help them.

We cannot ignore the complexity that individuals experience in making financial decisions, particularly given the financial stress that so many South Africans face. By helping individuals to make sensible trade-offs, all the stakeholders can better serve this country and its citizens.

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