Fleshing out the vision a better model

Could we do the same thing in South Africa?

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Changing the mindset around compulsory savings requires that we find a more effective way to use these savings to solve the problems that are uppermost to members' needs. This means recognising that while retirement savings are important, it's not the only important savings problem for South Africans.

As with the Singapore Central Provident Fund, we suggest focusing on the five things identified as critical and highly personal social protections:

We also understand that if we could provide an opportunity to solve for emergency savings at the same time, this safety net should help individuals stay focused on their longer-term savings objectives. To that end we add an emergency savings solution.

Getting members to buy in to this approach will demand two things:

1. We need to find a way to keep members committed to saving for the full duration, irrespective of the range of priorities they need to address. By keeping the amount an individual allocates to savings fixed, irrespective of the specific savings goal, members will have greater certainty about the amount of disposable income they have available for more immediate consumption needs. As such, the programme will need to guide members towards the optimal allocation for each funding imperative at the right time to deliver the most efficient use of available savings.
2. We need to create an environment where the savings experience also imparts knowledge and insights that enable members to be more fiscally responsible in managing the assets they build.

Bringing the dream to life

The lesson from Singapore was that getting people to engage with their priorities and actively manage them resulted in a more impactful and enduring outcome. Think of the programme as a lifelong engagement in personal financial planning. It's a programme designed to shape positive behaviours and habits which can then be shared across generations within the family or workspace.

We've learned through our *Benefits Barometer* journey that the most effective way to shape positive behaviours is to:

- make it as effortless as possible for people to do the right thing
- take away the distractions that cause people to abandon their programmes – so if debt is an issue, facilitate emergency savings programmes or create peer group support at work
- maintain a savings target, but instead of a replacement ratio, consider the minimum sum required for retirement. (In Singapore, that number was based on the income requirements for a lower-income couple after retirement. In South Africa, that number could be above the threshold used for the old person's grant.)
- start with the employment agreement and create a framework that allows employees to immediately see the long-term impact of their decisions around preservation, savings contributions and risk protections – before their contract is finalised
- get individuals to pre-commit to long-term automatic increases, as it's easier to get people to commit to something that will only unfold at a period in the future

- trigger these contribution increases automatically when people notice them least – such as after set bonuses or salary increases
- give members a framework to monitor their progress and test out different decisions and consequences
- create incentives for doing the right thing.

We've also come to appreciate that while employers have a sincere interest in their employees' well-being and financial stability, human resource departments are typically stretched. Ideally we want to create an enabling environment that doesn't impose additional pressures on the administration or human resources personnel.

Effectively we want employers to be able to simply tick a box that says: 'These are the benefits I would like to offer my employees.' Employees, in turn, would simply select how they would like their savings allocated and what sort of programmes would work best for them and their families. And we, as the benefits platform administrators, would effect and administer these choices.

We discuss exactly how we could solve for each of these savings options in the next few chapters.

> **Think of the programme as a lifelong engagement in personal financial planning.**

Modelling for impact

The key to making this type of arrangement work would be a particularly sophisticated modelling capability that would show members the trade-off implications each time they choose which savings goal they want to prioritise.

Practically, the model would represent a dynamic stochastic programme so that an individual can stress-test their choices or consider the impact of a different set of options on their total wealth as they move through time. The starting point would be to ensure that there would be funding for a base level of retirement income. But above and beyond that, the modelling exercise would help them assess how and when to best structure their contribution rates to meet other family priorities.

For example, if a member chooses to prioritise housing and pursues a pensionbacked housing loan and mortgage hybrid, how would that impact on the amount of savings they would have available for their minimum retirement income? Would they need to later arrange some equity release on that home to fund that minimum amount? If a family chooses education funding, at what point would they need to resume or escalate their retirement contributions to maintain their minimum amount requirement?

The good news is that such sophisticated modelling frameworks are beginning to emerge[1]. While they currently demand a particularly high level of computing power to cope with the mathematical complexity of the problem, we believe that these models are essential if we want to help individuals address what is perhaps one of the most difficult financial problems they must solve: "What will happen to me and my family's financial well-being in 30 years if I choose to follow this financial route and not this other one? What happens if I go in this direction for a while, and then, after 10 years, decide to veer off in another direction?"

A modelling framework such as this makes it possible for individuals to solve not just for retirement income, but for other long-term lifetime priorities – at the same time. This gives members the best of both worlds in decision-making: what's needed now and what will be needed in the future.

Concluding thoughts

Currently, National Treasury has been pushing for simpler and cheaper solutions to provide retirement funding. It's easy to understand why they should see this as an imperative given the current shortfalls to the system. As such, the industry has been trying to accommodate this need by cutting the servicing models back to the bone. But the harsh reality is that financial planning in its fullest sense is not a simple exercise. What we envisage here is something that is far more holistic.

This framework aims to simplify the decision-making process around financial planning for individuals and their families. What we're aiming for is a 'financial adviser in a box' solution for the broad swathe of South Africans who would typically never be able to access such an advice framework. With the model we propose here, we can be by their side for the duration of their financial journey. But let's start unfolding what that model should look like (and why) in our next six chapters.

References

1 Dempster, Kloppers, Medova, Osmoloky & Ustinov, 2016