[Fleshing out the vision a better model]

Education-the engine room for social mobility

South Africa | 06 June 2016 | Insight

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Financial well-being is a complex, intergenerational, intra-family problem. Employee benefits go some way to provide a safety net to dependants, but a higher priority for many families may well be enabling dependants to become future financial contributors instead of perpetual dependants. As such, people generally have a keener interest in upward social mobility than retirement savings.

More specifically, the demographic challenge for South Africa for the next 30 years will be the youth, not the aged. The need to fund for retirement pales in comparison to the scramble to enable and empower the next generation.

The primary catalyst for the desired social mobility is education. If we as individuals only achieve a limited degree of financial security from our own jobs, we can still hold out the hope that, with the right support, nurturing and education, our children can achieve even more. There’s a compounding element embedded in educational attainment, as shown on the right. From this perspective, improving the educational standing of every family member should come with a payoff.

The economic principle at work here is that schooling is an investment. In a complete market, you should theoretically be able to invest in education until the marginal private benefit from that investment equals the private marginal cost. But in South Africa, investing in education for mobility demands a very different appreciation. The payoff is far more complex[1].

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How does this work in South Africa?

South Africa's unique historical legacy throws some disturbing curve balls at the upward mobility dream. Three points in particular demand our attention and help explain that while investing in education may have a greater return in South Africa than other developing economies, getting the best payoff from such an investment is that much trickier.

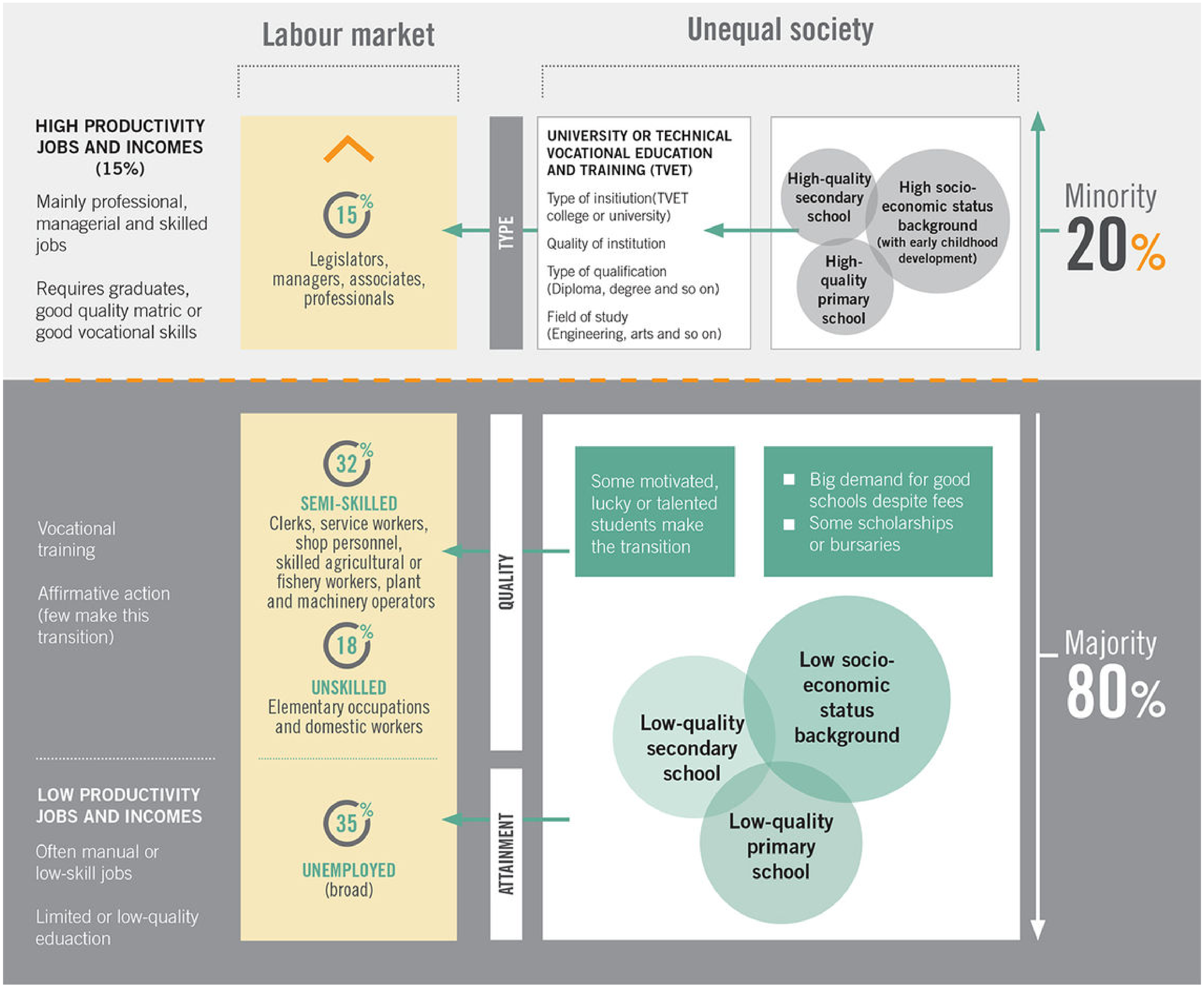
ONE:

To begin with, we can't assume a linear payoff between years of schooling and economic achievement. The wages of apartheid left the country with a deeply divided educational system, with only 25% of our public school systems considered functional. In his study on schooling in South Africa, Nic Spaul of Stellenbosch University describes this chasm as a poverty trap:

The tragedy is that these two systems continue to reproduce themselves despite the abolition of apartheid…. Although the top part of the education system and the labour market are no longer racially homogeneous (White), they are largely split along class lines. Those parents who can afford to pay school fees and send their children to well-functioning government or independent schools ensure that their children can get access to the top part of the labour market. Those parents who cannot afford school fees are excluded from these schools, often in informal ways. As it currently stands the dualistic South African education system is not an engine of social mobility but rather one of the key mechanisms through which an unequal society is replicating itself[2].

On top of this, access to good jobs is mostly through friends and acquaintances. It's not just about acquiring greater knowledge or skills that accounts for better prospects, it's about acquiring greater social capital or infl uence. Attending better schools allows for greater proximity to those valuable social networks[3].

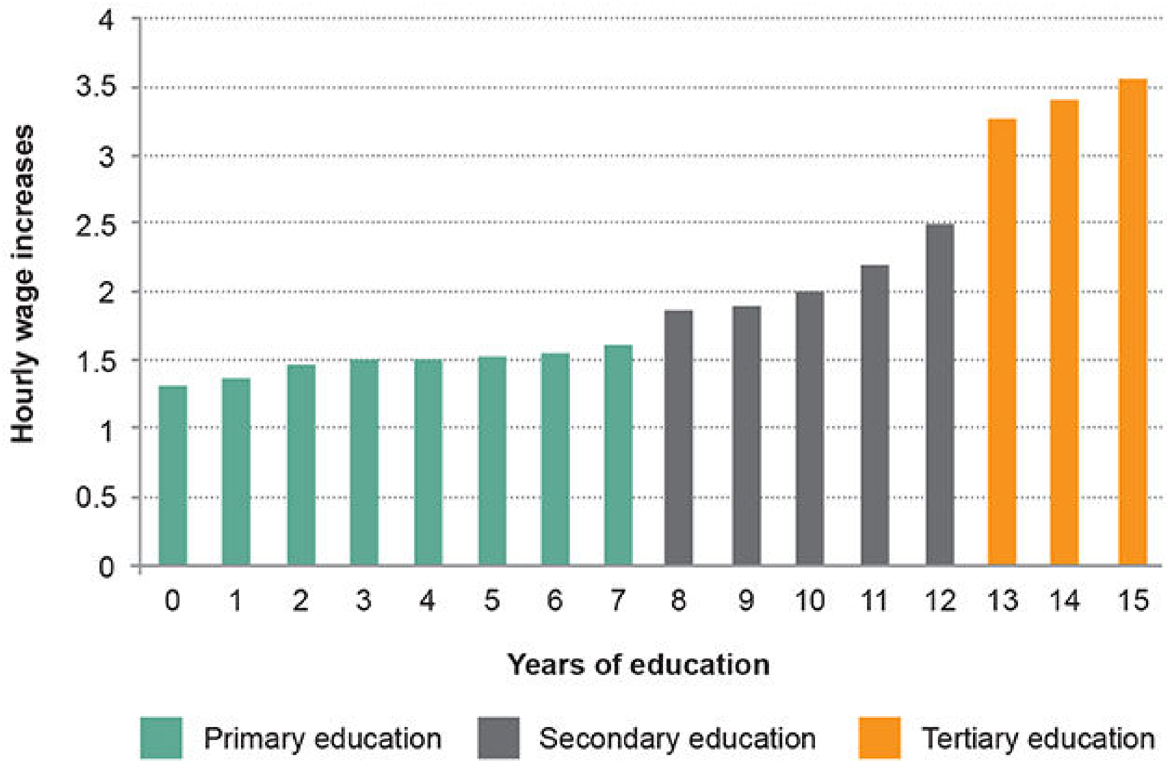
Spaul's infographic provides an excellent summary of the issues of this dual system with dual outcomes:



TWO:

The financial payoff from investing in education in South Africa is essentially convex. Students would need to have completed a substantial number of years of schooling before there's an adequate payoff for the investment. The following graph illustrates this point.

Translating years of education into hourly wage increases



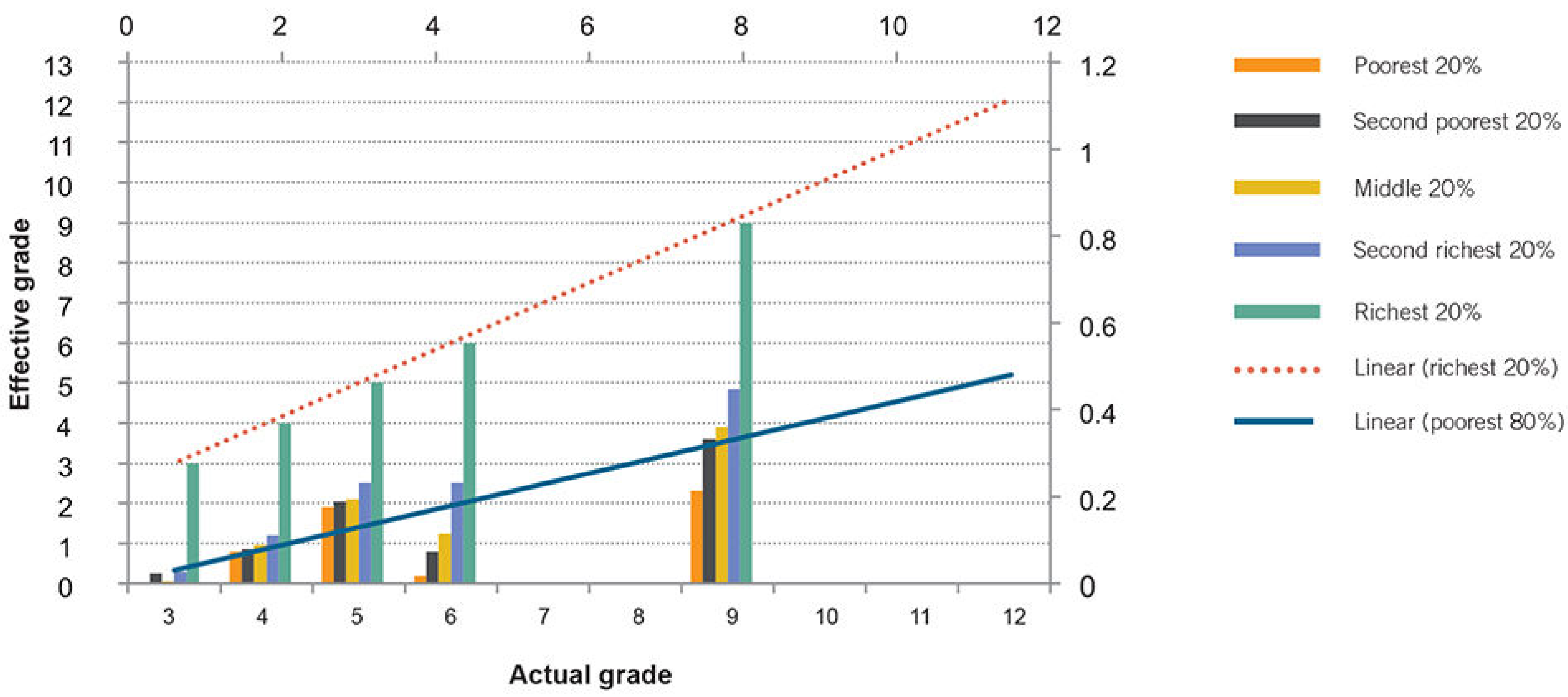
Source: Calculations on South African Labour Force Statistics, 2007^4

This accounts for why there is such focused attention in the media on matric results and university fees. As university appears to be the final launch pad for social mobility, this is where most parents give the greatest consideration to educational savings. By now, parents feel they should have some hint as to whether an investment in a child's further education is likely to pay off. But that conclusion may well be misplaced, as our third point suggests.

THREE:

In fact, research now shows that an investment at the earliest stages of education might provide the greatest payoff. Separate studies by Van der Berg, Spaull and Taylor confirm that educational inequalities from our two-tiered school system start as early as primary school. By Grade 3, these inequalities accumulated into an educational differential of more than three years[5]. This highlights the powerful influence that early cognitive development has on an individual's whole educational journey. By ninth grade the learning differential expands to five years. The following graph illustrates this impact, measuring the learning trajectories or tracks of wealthy and poor learners in South Africa by assessing their differential performances in maths exams. Maths scores appear to be reasonably good predictors of how people are likely to perform in the workplace.

South African mathematics trajectories by national socio-economic quintiles



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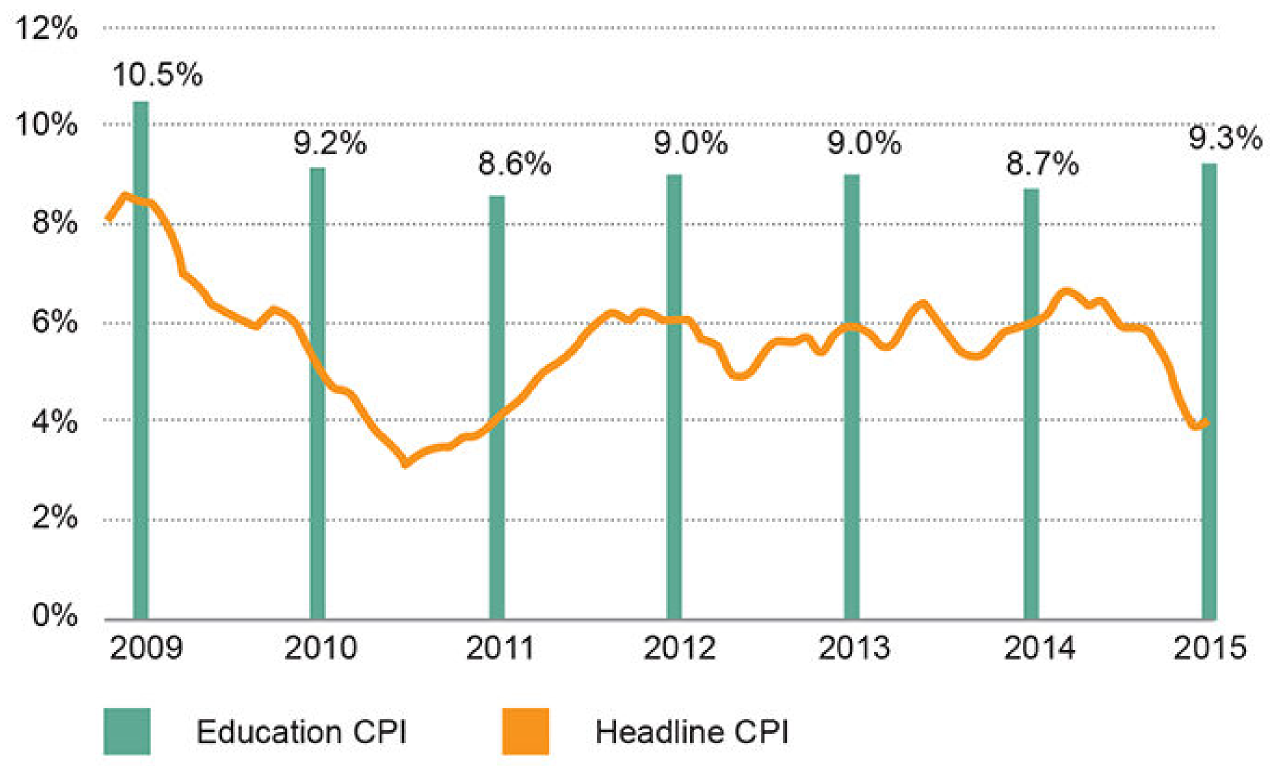
In summary, the consequences of not paying particular attention to children's education, especially in their formative years, is significantly greater in South Africa than other African or developing economies. But therein lies the rub. The last national household survey in South Africa revealed that almost two-thirds of children and youth cited lack of funding as the main reason for not attending school, despite a sharp increase in no-fee schools over the past few years. Registration fees (which have to be paid up front at high schools and tertiary educational institutions), transport and other education-related expenses continue to be obstacles for many disadvantaged South African families[6]. So, while we place a high value on education and the impact it can have on our children's lives, finding effective ways to fund these aspirations can be a real challenge, particularly if net income exceeds the limits of government grants and bursaries.

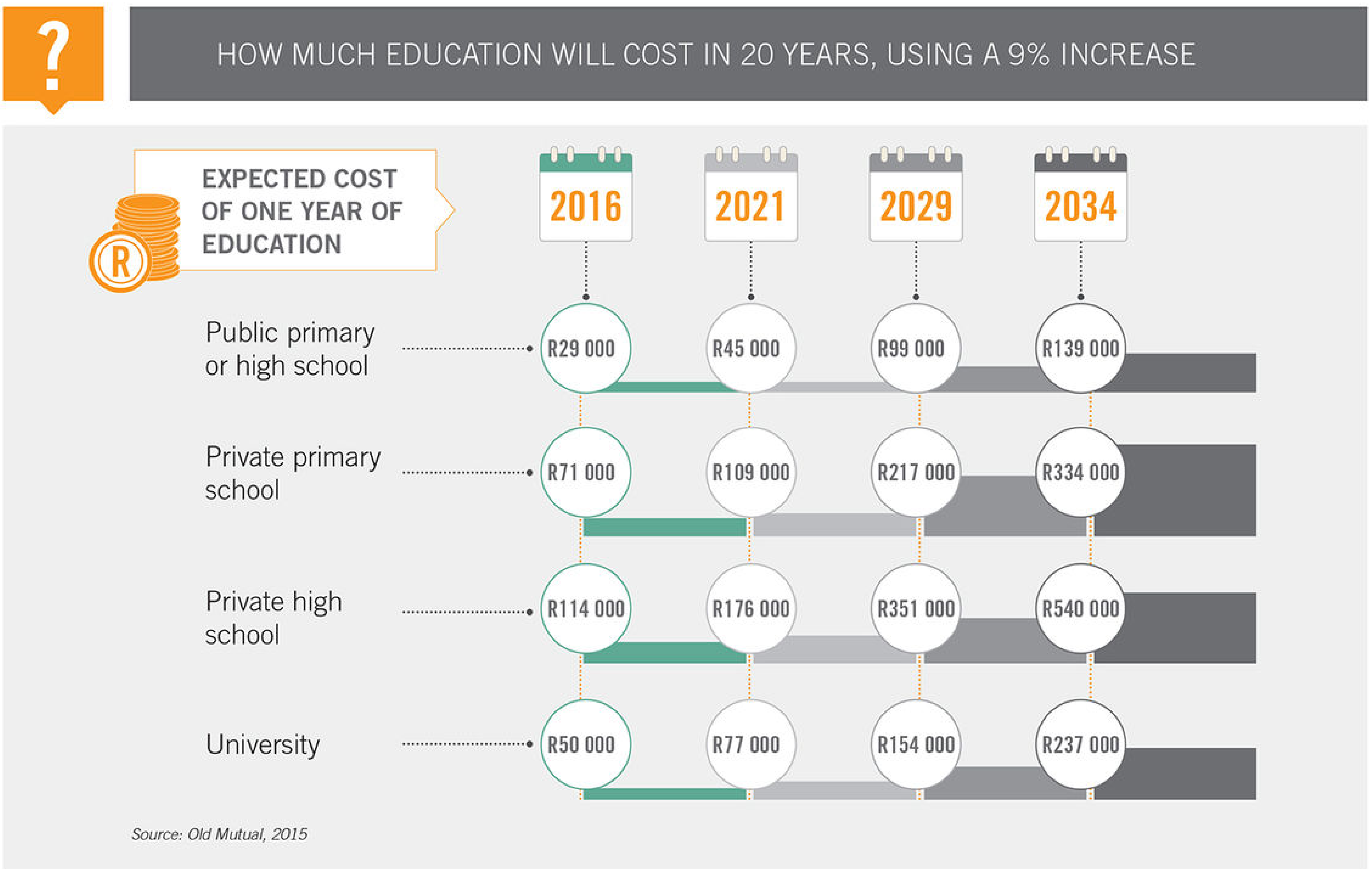
Cost continues to be an issue even for government schools. Educational inflation has tended to hover a good 3% above inflation since 2009.

The rising cost of education

Education inflation compared with headline Consumer Price Index (annual rate of change)



Source: Consumer Price Index, Statistics South Africa



Source: Old Mutual, 2015

These figures give us pause for thought, given that the current average cost for one year's education in **2016** at a public school (primary or high school) is about **R29 000**, while private high school fees vary around the **R114 000** mark.

As the table highlights, projections rise to **R45 000** for public and **R176 000** for private high schools by 2021.

This suggests that a savings plan for educational costs might be a high priority for many families.

COULD THE EMPLOYEE BENEFITS PLATFORM FACILITATE EDUCATIONAL FUNDING?

Here is the savings challenge. Educational funding competes head-on with saving for a deposit on a home, accumulating emergency savings, saving for retirement and a host of other early parental considerations. The question becomes: Is there anything that we could temporarily crowd out (and then force back in) to create the space to focus on educational funding? The answer, surprisingly, could be **your retirement savings.**

This is an interesting turnabout. While advocating emphatically that individuals need to start saving as early in their working careers as possible (and at the highest contribution rate), we can't deny that other priorities such as education or housing or emergency savings are equally important to the richness of their fi nancial journey. If funding education results in slightly lower replacement ratios at retirement, but enhances overall family wealth, is this hugely problematic?

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Diverting precious savings away from the retirement pool could be risky business, unless it's done in a highly controlled environment. We believe that the benefits platform that we are discussing in this book could provide just the necessary controls. The power of the programme is that it could either be entirely funded by the member, or employers might find it attractive to offer a matching strategy to members below a certain threshold.

Here's how we envisage the process

1. The member would commit to follow-through with each step of the educational savings programme. Once the member enters into the programme, each subsequent step would occur automatically.
2. At the outset, the member would determine the level of educational funding required, in how many years, and over what period. This could be done either with an online toolkit or through consultations with a financial well-being consultant.
3. The starting principle would be to set a reasonable contribution rate.
4. Savings could start at a trigger event: at the point of employment, marriage, birth of a child or at some early point in that child's development. The golden savings rule remains: the longer the savings period, the higher the probability of success.
5. This is one area where an employer matching programme would add significant value. When the member has reached their funding goal, the ongoing contribution will be allocated back into their retirement fund to catch up on their long-term savings.
6. What makes this programme effective is that because the overall savings rate remains constant throughout the retirement savings period, there's no new financial strain introduced to the family at any point. At the end of the day, the member ends up with a higher replacement ratio than if they simply diverted the money into education to pay for educational costs.

Concluding thoughts

The reality is: adequate funding to provide that critical educational boost at primary level is often beyond many young families' means. But a carefully orchestrated programme that allows a family to divert savings from retirement during those early years when that extra funding is required can still be achieved as long as those savings contributions are automatically channelled back to the retirement objective at that optimal transition point. In the next section we flesh this model out to illustrate how the varying savings goals can interact over time to allow us to solve for these differentiated priorities.

References

1 Behrman, Birdsall & Szekely, 1998
2 Spaull, 2015
3 Von Fintel, 2015
4 Van der Berg, 2013
5 Spaull, 2015
6 Mayer, Gordhan, Manxeba, Hughes, Foley, Maroc, Lolwana & Nell, 2011