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Previously Investec
Asset Management

Are you investing enough for your future?



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A key question that needs to be answered in any financial planning exercise is “How much do I need to save so that I can comfortably maintain my standard of living in retirement?”

Addressing this correctly and timeously is critical as pensioners have different needs (a regular income that ideally increases with inflation over time) and different risks (running out of money i.e. living too long) to other types of investors. There are also important psychological aspects that must be considered, given that it is unlikely that retirees will be able to live on the state older person’s grant (previously the state old age pension), go back to work or want to be supported by their family.

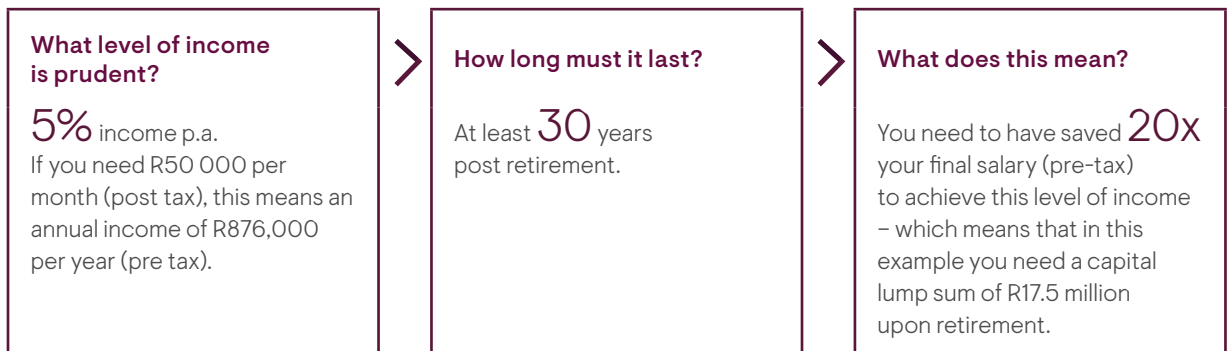
Ninety One previously completed an in-depth study into how investors should approach their retirement income provision. One conclusion highlights that choosing the right level of starting income is key to investors managing their risk of running out of money. In short, a retiree should elect a starting income level of no more than 5% of their retirement capital.¹ Other conclusions highlight the value of active management and the impact of volatility on income, and the importance of growth assets² for income.

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1. Jaco van Tonder, Ninety One: “A sensible income strategy is critical for living annuity investors.”
2. For more information, please see the following link to the dedicated “New approach to living annuities.”

Five and twenty are the numbers to remember

With this starting income level of 5% of retirement capital as your standard, we are able to calculate that you require a capital lump sum equal to 20 times your final salary to invest in an income-producing annuity on retirement. This is the amount required to generate an income equal to 100% of your final salary, post retirement (i.e. a replacement ratio equivalent of 100%). Drawing no more than 5% is considered likely to provide you with an inflation-adjusted income for 30 years, ensuring a comfortable retirement. Any capital lump sum of less than 20 times will result in a lower starting income (a lower replacement ratio) than your final salary and therefore you would need to reduce your monthly expenditure accordingly.



Saving enough is key to investors managing their risk of running out of money.

Time can be your friend – or your enemy. Let compound interest work for you.

Start early – but remember it is never too late

While knowing how much you require is critical, so too is knowing where you are on the path to this lump sum. Arriving at a sufficient retirement pot is a journey that takes a full working lifetime, as the following formulas illustrate. The impact of delay is considerable:

Starting at working age 20

15% of pre-tax salary x 40 years of employment = 20 times income required at age 60

- In this example, someone starts working at age 20 and saves 15% of their pre-tax salary every month for their entire working career. And, in the event they change jobs, they preserve their existing retirement savings. This proverbial unicorn is one of the minority who can retire comfortably at age 60.

Starting 10 years later

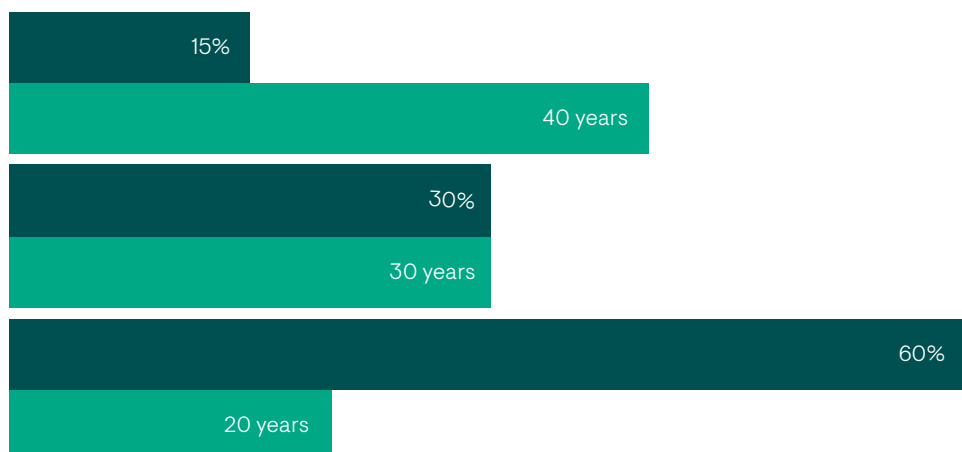
30% of pre-tax salary x 30 years of employment = 20 times income required at age 60

- A more realistic example is where someone does not start providing for their retirement from age 20 or does not preserve their retirement benefits when they change jobs in the first 10 years. They are then required to save twice as much of their pre-tax salary for the shorter 30-year period to achieve the same outcome (or retire at 70).

Starting 20 years later

60% of pre-tax salary x 20 years of employment = 20 times income required at age 60

- The more extreme outcome of the example above requires an improbable savings rate of 60% of pre-tax salary (or retirement at 80!).



- Percentage of pre-tax income to save to reach your goal
- Period to reach 20 times your final salary

Clearly, there are no quick fixes to a lack of retirement provision and, for many, very little likelihood of being able to comfortably retire at 60 unless you act wisely at the right time. However, it is never too late to start.

How do you know if you are on the right path?

Now that we have established how much you need at retirement and therefore what percentage of your salary you should be saving monthly, how can you assess your progress along the way? The following chart shows you what multiple of your current annual salary you need to have saved at any age between 20 and 60 to ensure a replacement ratio equal to 100%. We have also shown the multiples required for a 75% replacement ratio by way of comparison. A 75% replacement ratio may suffice for many retirees, depending on their lifestyle choices and financial obligations. Once retired, retirees do not typically contribute to a retirement fund anymore. Transport and clothing costs could come down, and they may be debt free, with financially independent children.

Figure 1: Milestones along the way to a comfortable retirement³



Source: Ninety One calculations.

So, by age 40, you should have accumulated retirement savings of approximately 5 times your annual salary if you are targeting a replacement ratio of 100%. Another interesting observation of this chart is the acceleration of capital values in later years, a clear illustration of compounding benefits. Note, while it took 20 years to accumulate savings of 5 times your salary it takes only a further 10 years for your accumulated savings to double to 10 times, and then only another 10 years for your accumulated savings to double yet again and reach the magical 20 times!

The value of active management should not be overlooked. A key assumption in our calculations is a portfolio return of 7% above inflation, which joins forces with compound interest and your contributions to deliver your lump sum available at retirement. With this return, 40 years of saving 15% of your pre-tax income should see you retire comfortably, drawing 5% per annum from your savings. However, if returns are 2% higher, at CPI + 9%, you'll have saved 35 times your final salary.

3. Assumptions: 15% of pre-tax salary saved for 40 years; salary increases at CPI+1.5%; portfolio return (whilst saving for retirement) = CPI+7% p.a.

What role can Ninety One play?

Given the importance of retirement provision, the best approach is to seek professional financial advice. As a dedicated active manager, Ninety One offers a comprehensive range of local and offshore unit trust funds, certain of which have the strong growth engine bias that is required by investors saving for retirement.

The Ninety One Opportunity Fund specifically targets inflation plus 6% per annum over rolling 3 to 5 years, and importantly no negative returns over rolling 24 months. Given the challenging investment environment, Portfolio Manager, Clyde Rossouw, emphasises the importance of maintaining a balance of exposures that offer protection in several different investment environments. The correct forecasting of complex global macro outcomes is almost impossible (as recent events bear testament to). Even if it were, positioning an investment portfolio precisely for such an outcome is even more challenging. We therefore do not believe it appropriate to position the portfolio for any particular event. Rather we maintain a balance of exposures which offers protection against a range of potential outcomes.

The Ninety One Investment Platform can also assist investors to grow their retirement nest egg via the Ninety One Retirement Annuity and, importantly, preserve their accumulated retirement savings via the Ninety One Preservation Funds if they have to leave their pension or provident fund for any reason, such as changing jobs.

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Contact information

For more information and assistance with investing, call the Advisor Service Centre Tel: 0860 444 487

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Alternatively, please contact your Ninety One investment consultant.