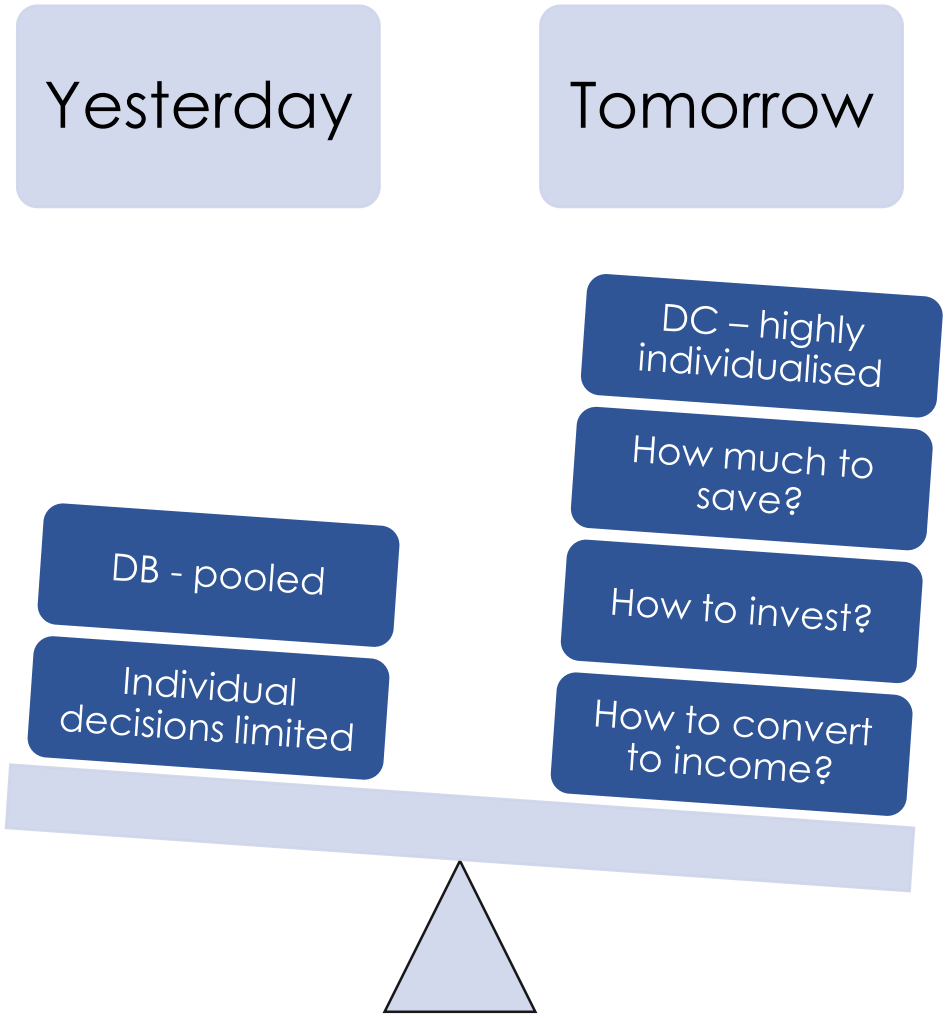
THE ROLE OF DEFERRED ANNUITIES IN POST-RETIREMENT INVESTMENT STRATEGIES

ONLY 6% OF SOUTH AFRICANS RETIRE COMFORTABLY

WHY



"The default regulations will require that fund trustee boards assist members during the accumulation and retirement phases."

National Treasury, 25 August 2017

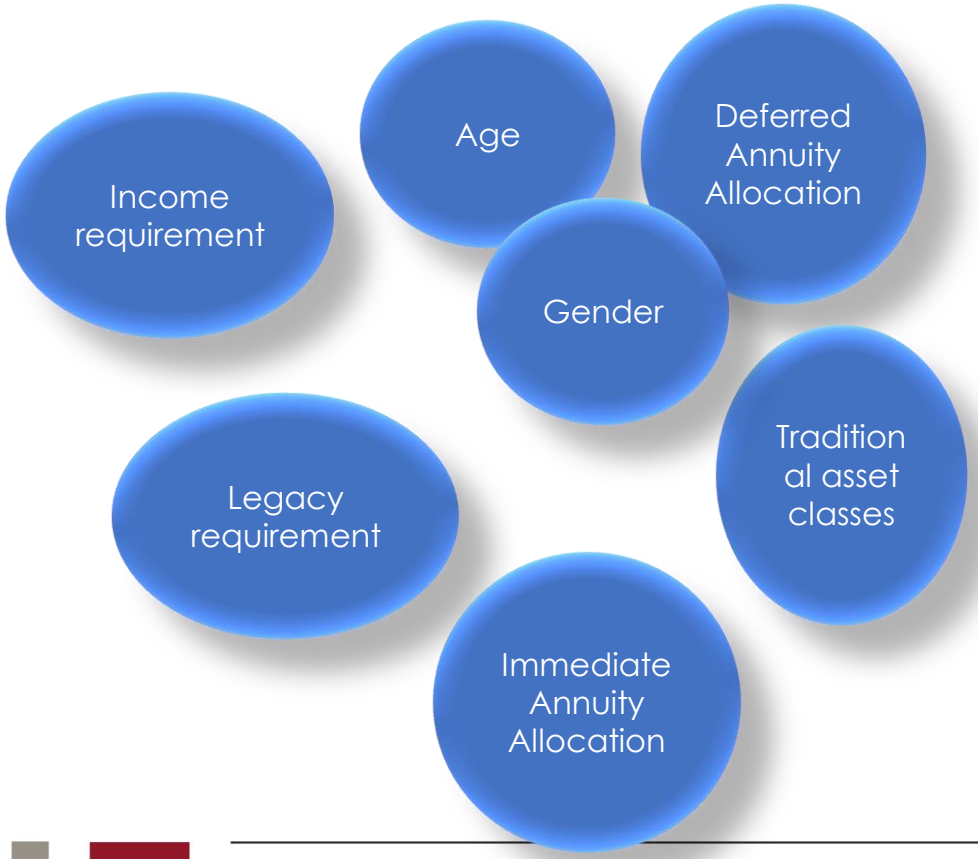
DEFERRED ANNUITIES POPULARISED GLOBALLY

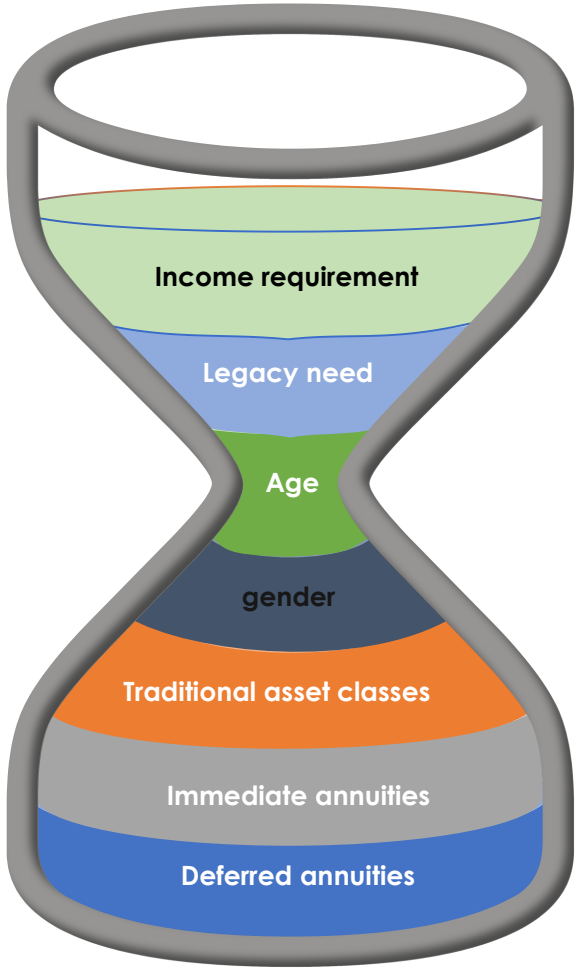
International vs South African context?

Existing literature providing mixed views

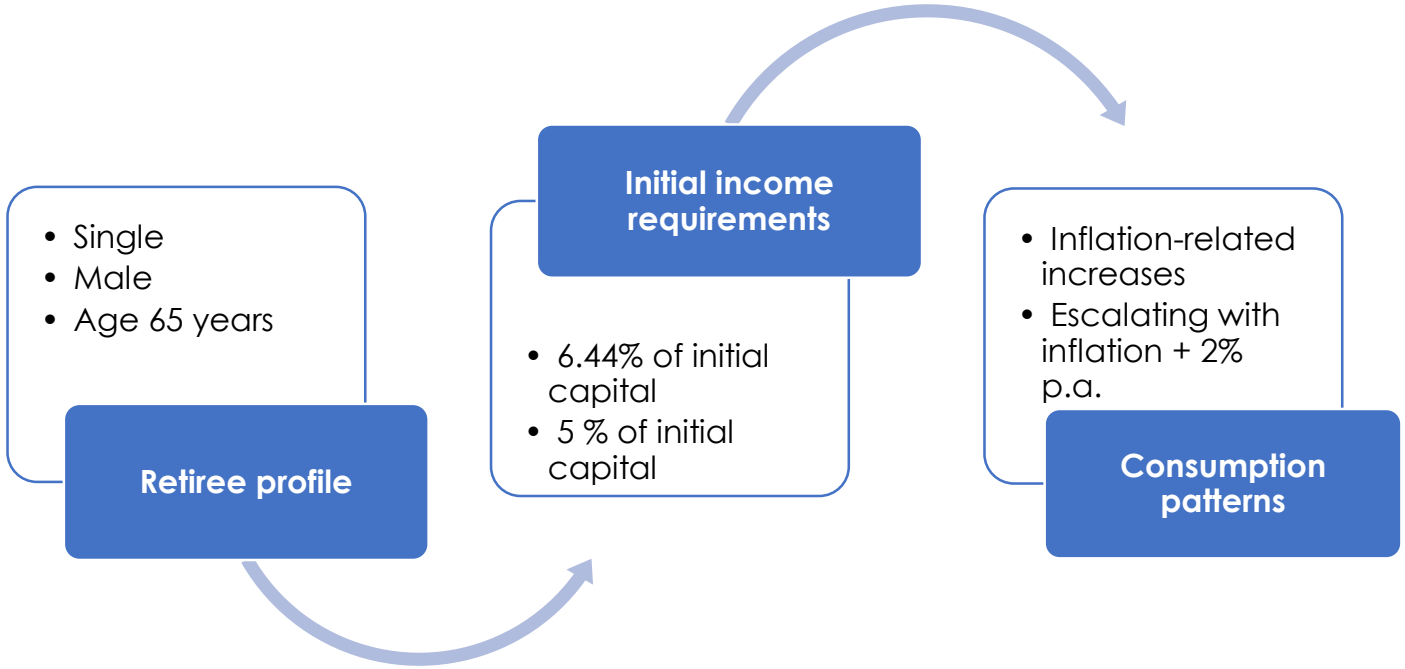
Limited research and market development in SA

EVALUATING WITHIN A GOALS-BASED FRAMEWORK

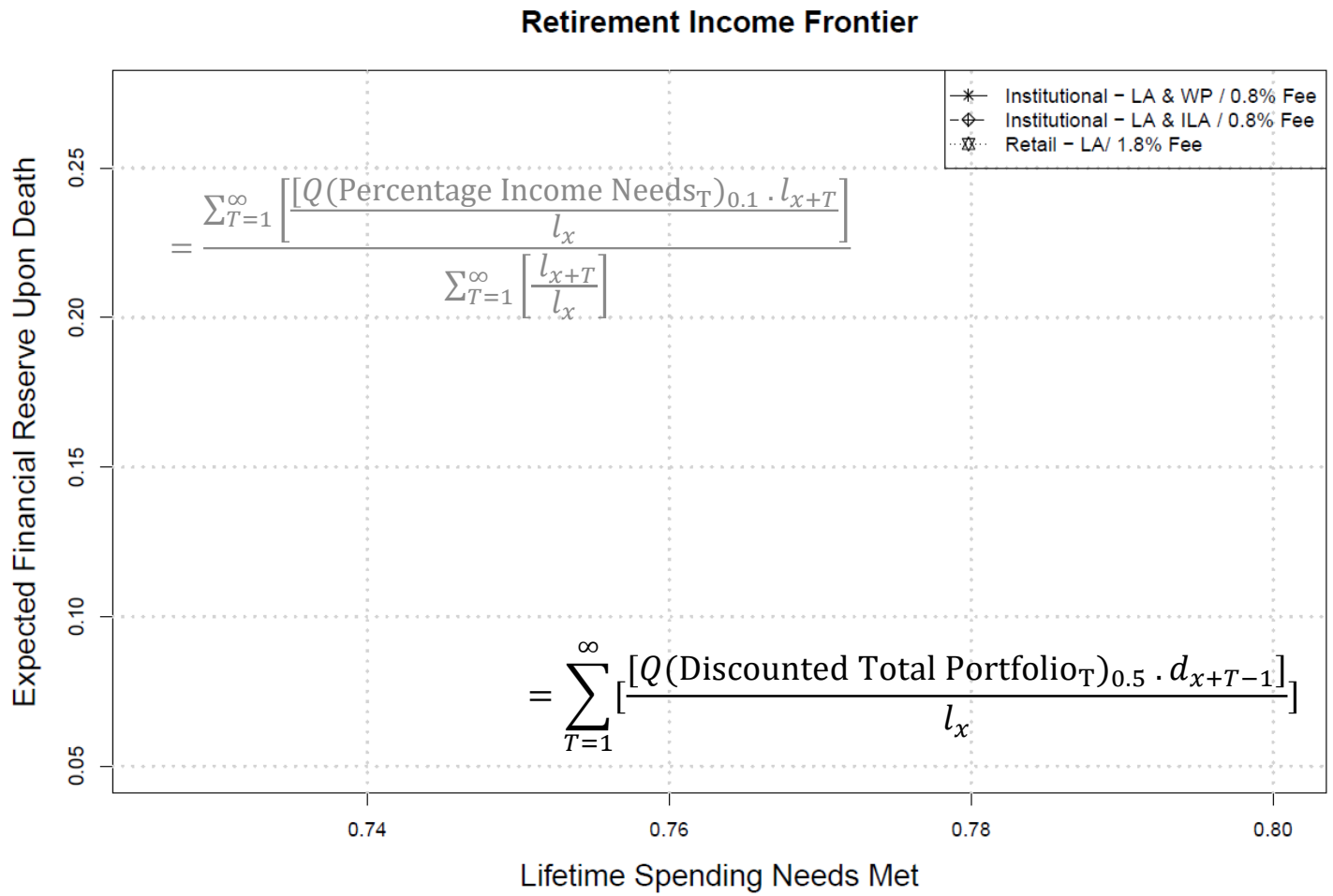




SCENARIOS CONSIDERED



RECAP OF RETIREMENT INCOME FRONTIER



Key features

- *Consumption framing*
- *Goals-based*
- *Individualised*

ACTUARIAL SOCIETY OF SOUTH AFRICA

INCLUSION OF DEFERRED OR IMMEDIATE ANNUITIES IMPROVES OUTCOMES

Current approach ~90% of retires invest in traditional living annuities with no longevity protection is sub-optimal

- Improved lifetime spending needs
- Improved expected legacy values
- Greater asset allocations to growth assets possible

Additional return from mortality credits

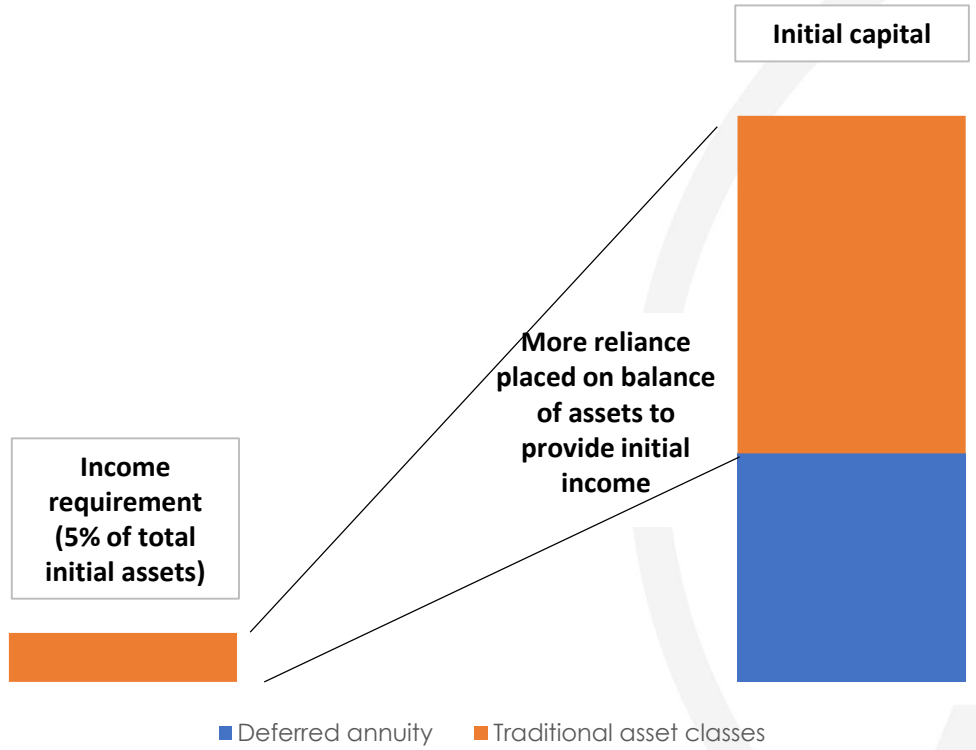
- ***2.8%*** *p.a. over 10 years*
- ***3.9%*** *p.a. over 20 years*
- ***4.9%*** *p.a. over 30 years*
- *Immediate annuity*
- *Basis : Male, PA(90) – 3*

Mortality Credit Definition (www.annuitydigest.com):

The mortality credit is also known as the mortality yield. With a participating annuity, premiums paid by those who die earlier than expected contribute to gains of the overall pool and provide a higher yield or credit to survivors than could be achieved through individual investments outside of the pool. The mortality credit increases significantly with age and hedges longevity risk, often creating a return that would be impossible to match in the broader financial markets.

IMMEDIATE ANNUITIES MORE OPTIMAL THAN DEFERRED ANNUITIES IF NO CONSTRAINTS IMPOSED

- Mortality credit benefit applies across more income stream payments from earlier date
- Sequence of returns risk reduced when annuitizing earlier
- *An implicitly modelled guarantee included where more of the initial income can't reduce in nominal terms.*



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WHERE CONSTRAINTS IMPOSED ON INITIAL CAPITAL TO ANNUITISE : DEFERRED ANNUITIES MORE OPTIMAL IN SOME CIRCUMSTANCES

- Deferring income to start from age 75 years preferable to deferring to 85 years
- Desirable for pensioners who are better funded for retirement
- Not desirable for pensioners who are poorly funded for retirement
- From behavioural finance stance, may be attractive to impose constraint on initial capital annuitised
- But, strictly speaking, imposing constraint results in less optimal lifetime spending and expected financial reserves compared to an unconstrained strategies
- The decision to defer the purchase of an annuity is sub-optimal, both in terms of behavioural finance as well as in terms of the retirement income frontier framework

ACTUARIAL SOCIETY OF SOUTH AFRICA

WHERE CONSUMPTION INCREASES IN RETIREMENT : IMMEDIATE ANNUITIES STILL MORE OPTIMAL VS DEFERRED ANNUITIES

- Literature on retirement spending reach differing conclusions
- SA research limited
- Inflation + 2% p.a. pattern assumed to test sensitivity to spending patterns

"Consumption needs at advanced ages would need to increase substantially (and in a step-wise fashion) for deferred annuities to be considered appropriate relative to immediate annuitisation."

Does the "Retirement Spending Smile" exist in SA?

TO CONTINUE OUR DISCUSSION...

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