Nearing retirement … what now?

Various pension products are available when you retire. **Make sure you choose a product that makes the best provision for your personal needs.** Here's what you should know.

At retirement you have to purchase a pension product with your accumulated fund value in the Sanlam Staff Umbrella Pension and Provident Funds (SSUF). But how do you choose between the many different types of pensions or annuities?

Ask your financial adviser to assist you to understand the characteristics of the different types of pensions, particularly the associated risks of the investment-linked living annuity (ILLA).

An ILLA is very different from a traditional insured annuity and requires a different investment strategy during the years leading up to retirement. If you plan to purchase a living annuity or ILLA when you retire, you should adapt your investment strategy accordingly.

Traditional insured versus an ILLA

A pension or annuity is an income that is paid from a pension fund, usually for the remainder of your life. In certain circumstances the income or a portion thereof is continued for your dependants.

At retirement you need to address various issues when you select a pension. The most important one is the level of income required. Prepare a budget that's carefully considered and does not include unnecessary luxuries, as insufficient income will be a difficult problem to address at that stage.

Some other considerations are:

- **Longevity** – The longer you live the more savings are required. Some pension products, like traditional insured annuities, reinsure the risk of reaching an advanced age with a life insurer, whereas in an investment-linked annuity the risk of longevity remains with the member.
- **Investment risk** – The investment of your pension provision has to be made in a product provided by a registered life insurer. With certain products the life insurer takes the investment decision and risk and with others you carry the risk of sufficient income and/or capital loss.

- Inflation – You should protect your pension against the ravages of inflation, which reduces the purchasing power of your pension.

  Historically investments in equities (shares) and property have proved to be the best protection against inflation but the volatility in prices and income levels may not be sufficient.
- Costs are becoming a more important factor in a low-inflation environment.
- It's also possible to provide for your dependants in various ways.

What is a traditional insured pension or annuity?

A traditional insured pension or annuity can be either:

- A guaranteed annuity – an annuity that is contractually subject to a guaranteed increase at a fixed rate, which may be zero, over the full term of the annuity; or
- A with-profit annuity – an annuity where your pension increases are linked to the performance of the underlying investments. When investment markets boom you can expect above-inflation pension increases but when they are down you could lag behind inflation.

Over time a with-profit annuity is likely to increase at a rate better than inflation because a proportion of the underlying assets of the investment portfolio is invested in shares, which have historically provided above-inflation returns.

What is an ILLA?

An ILLA is a flexible investment product rather than an annuity, even though the purpose of the product is to provide an income.

	INSURED PENSIONS	WITH-PROFIT PENSIONS	INVESTMENT-LINKED PENSIONS
Characteristics	→ At retirement you decide on a fixed rate of increase. The higher the rate of increase, the lower the initial pension. → The category includes a wide range of products offering various choices, such as: • guaranteed capital • a minimum guarantee period – for example, five years or 10 years • spouse's pension, et cetera.	→ Purchased at a fixed purchase rate. The pension increases will be the difference between the declared investment rate and the purchase rate. The higher the purchase rate, the higher the initial pension and the lower the future increases. → When the pension is purchased, the member has a choice regarding a minimum guarantee period and a spouse's pension option.	→ You obtain your own investment account and choose the portfolios in which your retirement capital is invested. You choose the size of your pension by means of a withdrawal from the capital at a rate of between 2,5% and 17,5% a year. → You may nominate a person (such as your spouse) to continue the pension after your death or to receive the balance of the capital.
Risks	→ Future rate of inflation is unknown. For example, a member may choose a 5% rate of increase and inflation may rise to 15%. → If interest rates are low when the member retires, it is expensive to purchase such a pension – the pension per month is lower than it would have been in circumstances of high interest rates.	→ In times of poor investment performance pension increases may be low or no increases may be granted. The pension may, however, never be decreased and an increase already granted cannot be revoked.	→ You carry the full investment risk. → If you withdraw a pension at a higher rate than the investment return earned on the capital, the capital and future investment returns will decrease and the pension may even become insufficient. → Investment decisions are important and a drop or volatility in investment markets may have a negative effect on the pension.
Benefits	→ You have certainty about future pension payments – you know what the increase will be, what happens at death, and so on.	→ Because increases are linked to investment returns, it is related to inflation to the extent that the return exceeds the purchase rate. → The pension increase is to a certain extent (according to the purchase rate) linked to the investment return earned by the underlying assets. → The pension can never decrease, only increase.	→ A person with good investment expertise retains control of the investment decisions regarding his or her retirement capital. → You choose the level of pension and increases you receive – within the guidelines laid down by the authorities.

** Please consult with a suitably qualified financial adviser about which pension suits your particular circumstances.*
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