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Retirement funding: what's your number?

We are constantly measuring our wealth and our health. The number of steps we take per day, our average heart rate per exercise session, our Smart Shopper points, rewards, eBucks, share portfolios … You name it, we measure it.

But how often do we check whether we're on track for one of the most important events of our lives: retirement? And, more importantly, do we know what measure to use?

The 2017 Sanlam Benchmark Survey found that, among retirement fund members, the burning questions in the financial planning process are:

• Exactly how much should I retire with?

• How much must I save every month or year if I want to retire comfortably?

Why are people so confused?

According to the Benchmark report, all the retirement funds surveyed have a target pension, expressed as a net replacement ratio (NRR), that trustees work towards achieving.

A NRR is the percentage of a member's pre-retirement income that is paid out by a pension plan at retirement, divided by his or her pre-retirement salary. It is a common measurement that can be used to determine the effectiveness of your pension plan.

But how effective is this measure really if 40% of the funds included in the survey believe that the NRR is not suitable for determining whether a member is on track for retirement? The main reasons for this response are that members do not understand the measure, and too many variables and assumptions are used to calculate the ratio.

One of the biggest areas of concern is that most funds define

Rands & Sense

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pre-retirement salary as "pensionable remuneration", which can be any percentage and is normally less than 100% of members' total remuneration.

It therefore could be argued that the NRR is not a suitable measure for determining whether members are on track for retirement. So what should your number be?

TRY THIS NUMBER

One number that is easy to understand is to express your retirement savings as a multiple of your current salary at different points in your working life. The multiple of your salary that you should have saved is based on the following assumptions:

• You retire at age 65;

• You save 15% of your annual salary (including your annual bonus/13th cheque) each year;

• Your investment earns a return of 10% a year;

TABLE 1

Years worked	Multiple of current salary saved
5	1.2
10	2.3
15	3.7
20	5.3
25	7.2
30	9.4
35	12.0
40	15.0

TABLE 2

Age at which you start to save for retirement	Percentage of salary that you must save
25	15%
35	24%
45	43%
50	60%

• Your salary increases by 6.5% a year; and

• If you are married, both you and your spouse contribute towards retirement savings.

Based on these assumptions and that you should have saved 15 times your final salary by the time you retire, Table 1 (above) sets out some goalposts on the road to retirement.

Currently, for each R1 million that a 65-year-old member saves, a man will receive a monthly pension of about R6 000, while a woman (because she is expected to live longer) will receive about R5 400, growing with inflation every year. So, if you want to invest in an inflation-linked annuity at the age of 65, you will need to have saved 15 times your final salary by 65.

Table 2 sets out the percentage of your salary that you should save if you start saving at different stages of your life.

As the table shows, if you haven't started saving at age 25, saving 15% of your salary will not enable you to achieve a multiple of 15 times your final salary at retirement. Late starters have to save much more every month.

Which products should you use to save for retirement?

You may consider a traditional pension or provident fund, and supplement it with a retirement annuity, a tax-free savings account, retail government bonds or an ordinary unit trust fund. This combination will give you more flexibility in terms of investment choice and the ability to access your investment.

BOOST YOUR SAVINGS

There are other ways to boost your retirement savings:

• The first golden rule is never to cash out your retirement savings when changing jobs. This remains the biggest mistake that members make.

• Do not be tempted to access your savings to pay off debt, buy consumables or upgrade your lifestyle.

• At retirement, do not take the one-third cash lump sum, because your long-term need for a higher monthly pension is more important than the luxuries you can buy.

• Know exactly what percentage of your monthly salary and annual bonus you need to save to reach your retirement goal, and set up a monthly debit order so that the money goes off your salary before you are tempted to spend it.

• Invest wisely and tax-efficiently, and know exactly what you are paying in fees.

• Obtain advice from a financial adviser with the Certified Financial Planner accreditation.

• Investing for retirement is a long-term goal, so make sure you are sufficiently invested in aggressive assets (such as equities or listed property) so that you can earn inflating-beating investment returns of at least 10% a year after fees.

• If you don't have a goal, there is nothing to aim for. Make sure you know what your "final number" is, and make every effort to stick to the plan.

These rules of thumb may not account for everyone's personal circumstances. A sudden spike in your salary may mess up your multiples for a year or two, but be sure to have your retirement-saving goals in place. Allocate any extra cash to your retirement savings and not to enhancing your lifestyle.

A disciplined approach to saving for retirement is the best gift you can give yourself in your "golden years".

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