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MICRO-SOLUTIONS

Designing pension products better suited for our society

Most retirement savings products are aimed at people with a consistent income and who work in the formal economy, thereby excluding the vast majority of South Africans. By addressing this, the burden on the state can be decreased and the wellbeing of the country's growing number of pensioners improved.

Economic estimations show that the size of the informal economy is approximately 7% to 12% of our entire economy. Those within the informal economy commonly face exclusion from financial market access. This is not just with regard to access to basic financial services, but in relation to products that will benefit household financial stability in the long run.

Statistics South Africa attributes almost a fifth of total employment, or 2.4m jobs, as coming from the informal sector. Characteristics of workers in this sector include inconsistencies in income streams, limited financial literacy levels, and limited, if any, access to pension or provident funds.

The current pension burden and cash transfers the state makes is 3% of GDP, or R128bn in 2016. Much of this is towards old-age grants, the highest contributing factor at R53bn, or nearly half of the state's commitment. It has grown significantly in the last nine years, up from R21bn in 2008. Simply put, more households entering into retirement are reliant on the state for support. This is unsustainable in the environment of low growth, high unemployment and fiscal consolidation.

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Savings challenges

We know that the average South African household does not save, with a current savings rate of 16%, dwindling from a high of 37% in 1980. Households save inadequate amounts for their retirement, but this could also point to a systemic problem. Are there suitable financial products to absorb postponed consumption in the South African context? This is a relevant question for all African economies that have a combination of formally and informally employed making up their economically active populations. In some African economies it is skewed heavily towards informal employment.

A large majority of those working do not save, but even among those who do, the amounts are inadequate for retirement. Statistics from Old Mutual show the same number of people save for retirement as do for funeral expenses. This points to possible systemic issues when looking at the structure of the economy. Financial literacy and disposable income levels are direct determinants to savings contributions.

But looking at the supply side of the market, one has to question whether there are products that a domestic worker, security guard or seasonal farm worker can make use of for long-term savings towards retirement. Do financial services companies place enough emphasis on developing flexible and relevant savings products for retirement? There is certainly nothing similar to the funeral policies developed and strongly marketed to middle- and low-income households, with the focus on tombstones, coffins and airtime or groceries when a loved one dies.

The existing products range from provident or pension funds that are suitable for the formally employed sections of the economy, to retirement annuities with their tax benefits. This leaves low-income households or informally employed masses of people out in the cold. These are the same individuals who will likely seek state support in the medium to long term, heavily burdening the fiscus and future generations.

Whose problem is it to help the unbanked without savings?

The financial services sector needs to consider offering micro-pensions to enable access to financial products for those who are not included in the formal economy, as well as low-income households in the formal sector. These are typically pensions that are structured for individuals with irregular income, small amounts, and aimed at savers with limited financial literacy facing even lower chances of accessing conventional financial products to save for retirement.

The role of the state in this regard is to create not only a conducive environment, but policy encouraging the development of micro-pensions. After all, it is the state that will foot the bill of non-savers in the end. It is likely to be funded by the non-contributory pillar of pension schemes, further putting pressure on the fiscus in the next 30 to 50 years.

At the current R128bn cost of cash transfers, projections of how this could increase with worsening growth projections, heightened pressure on unemployment and increased inequality does not bode well for balancing fiscal pressures in the long run.

We also have inadequate savings to finance (or bolster) investments required to boost overall economic growth. As a country we remain and are reliant on highly volatile

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