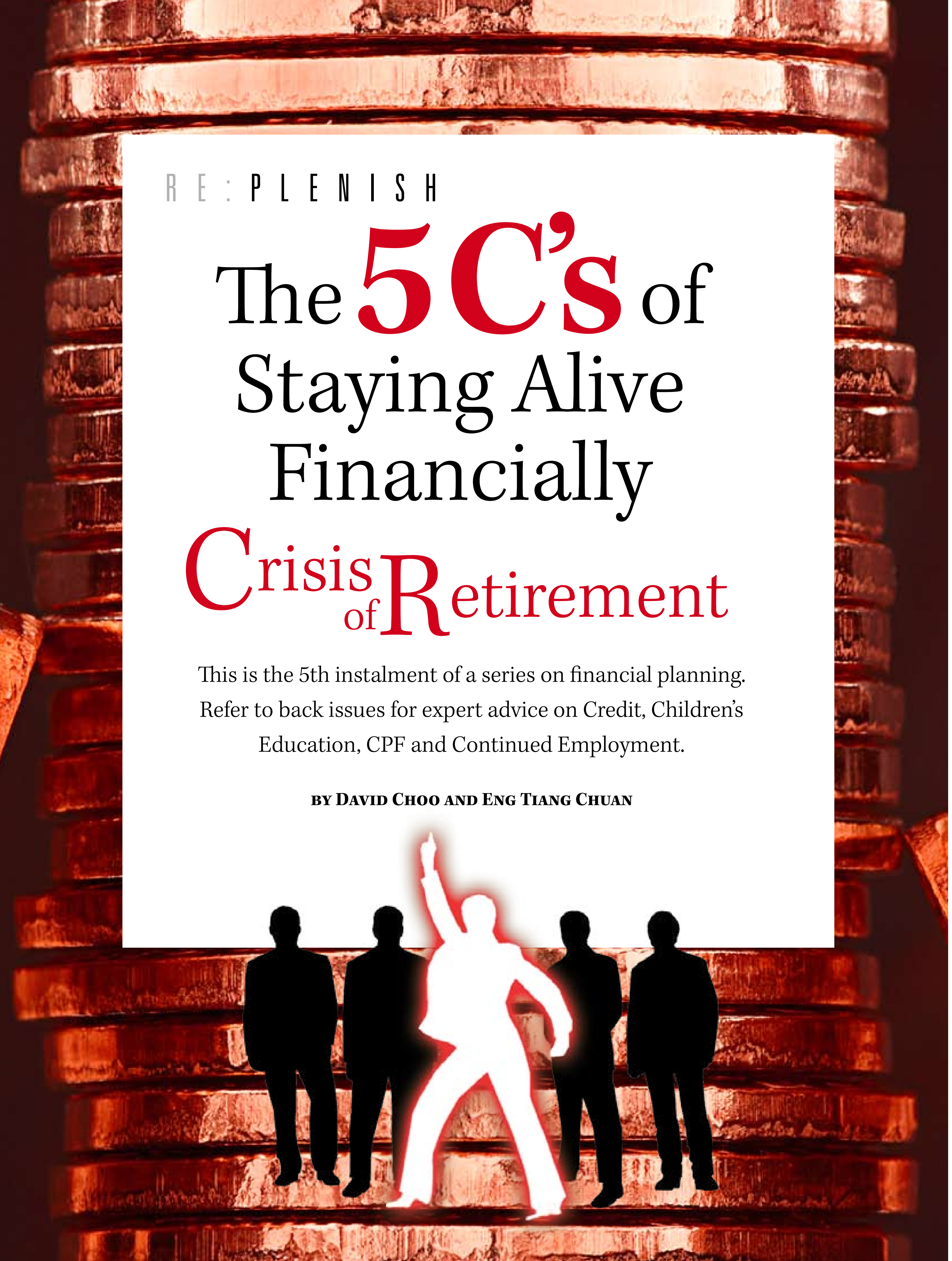

RE:PLENISH

The 5 C's of Staying Alive Financially

Crisis of Retirement

This is the 5th instalment of a series on financial planning. Refer to back issues for expert advice on Credit, Children's Education, CPF and Continued Employment.

BY DAVID CHOO AND ENG TIANG CHUAN

Singapore's rapidly aging population has been described as a crisis which has necessitated the attention of a minister to try to avert or at least mitigate it.

The metaphor of a time bomb is even more alarming, but not out of place, as the majority of Singaporeans grapple with a long retirement with insufficient funds. "Retirement" is supposed to be shangri-la conjuring images of relaxing times and holidays with sun, sand and sea for the outdoor type, and lying in bed till late, jacuzzi and mahjong for the sedentary. But for the unprepared, retirement often turns out to be the phase of life which is sans teeth, sans hearing, sans health, sans money, sans everything.

The retirement crisis arises mainly because the national savings scheme (CPF) is not sufficient to provide everyone with a comfortable retirement. The average CPF balance at age 55 was only $66,000 in June 2007. It is estimated that only 60 percent of those reaching age 55 in 2013 would have $67,000 or more in their Ordinary Account and Special Account, and 25 percent will have less than $40,000. Media reports have it that the average monthly disposable income (after paying for household expenses) of retirees in Singapore today was only about $100!

How can you ensure that you do not end up having time but not enough money to enjoy your retirement? Let's take a look at the four P's of retirement – principles, plans, provision and pitfalls.

Principles

There are five commonsense principles which must be practised in the area of retirement planning:

- Take responsibility for your retirement.
- Take into account the much longer average lifespan for the present generation – 80 years for male and 84 for female.
- Factor in inflation.
- Exercise some risk management to prevent financial pitfalls due to certain crises.
- Start early.

Except for the super rich, the typical Singaporean must be prepared for the multiple whammies of longer life expectancy, rising inflation especially of medical expenses, little government aid, unlikely help from children and competition for what retirement savings there are. Imagine having to cater for another 30 to 40 years of retirement without any more earned income. Imagine that inflation will eat into your retirement savings unless you have investment returns to counter it. And imagine you do not have help, or you prefer to turn away help from unwilling care providers. Unimaginable? Well, you'd better started planning for your own retirement.

Plan

The mathematical approach to retirement planning seeks to determine the lumpsum amount you need at the start of retirement to see you through your retirement years. (Also see other story "Living on 70 Percent of Your Pay".) You factor in your expected lifespan or number of years in retirement, the amount needed per month and the inflation rate and investment rate.

For example: Mr Tan, now 40, who wants to retire at 60 and expects to live to 85, reckons he needs $2,000 per month and factors in inflation rate at 3 percent and investment rate of 4 percent. Based on these figures and expectations, he would need $962,654 at age 60.

The savings and investment plan would be to determine what Mr Tan now has to his name (his useable asset minus his liabilities, excluding his owner-occupied property) and to compute what he has to set aside each month to achieve the required $962,654. If Mr Tan now has $50,000 savings and he factors in an investment return of 4 percent to age 60 for his savings and his regular savings plans, then the additional monthly amount that he needs to set aside is $2,314.

Mr Tan now needs to work out how he can set aside this amount and the best way to invest it. He can choose from among a wide range of products – endowment, investment-linked products, unit trusts, equities, bonds, etc. It is best to consult a financial planner or adviser who can not only provide good advice but also offer a wide range of choices for consideration.

However, while keen to achieve a good investment return, it is important for Mr Tan not to risk losing his capital as it is meant for his retirement.

Provision

The most challenging part of retirement planning is not the mathematics, or choosing the products, it is how to set aside the required savings regularly. Those who start planning and setting aside for retirement at an early age have the "miracle of compounding interest" working for them and so have more time to save. This translates to a smaller sum required.

For Mr Tan who is starting his retirement savings at 40, he has only 20 years left. Perhaps the greatest challenge is the choice between present enjoyment and delayed gratification. The majority of Singaporeans need to reduce their present expenses (on food, clothes, holidays, cars, entertainment, etc) in order to provide for future expenditure. Some people find the two bins illustration helpful. One bin is labelled "PRESENT" and the other bin, "RETIREMENT". Each month you put a portion of your salary or income into each bin according to your budget and retirement plan.

Pitfalls

One does well to bear in mind that the best thought-out plan is not devoid of pitfalls. Common "pitfalls" include unforeseen or unplanned events which cause income to dry up (divorce, job loss, disability, investment failure – remember the Lehman Brothers saga?) or expenses to increase (medical, legal suits, children's education especially in private universities or overseas).

A sound risk management approach is not only prudent for institutions but also for individuals and families. Medical expenses have wrecked many families and individuals but can be taken care of by approved shield plans paid from Medisave. Disability income policies can replace income loss due to total disability and professional indemnity policies can cover legal liability losses. The ElderShield and MyCare products give some protection against certain disabilities.

CPF, which is the pillar of many Singaporeans' savings plan, allows the individual to invest a portion of his Ordinary Account and Special Account under the CPF Investment Scheme. Unfortunately, many have not invested well and sad stories are told of many who needed money and have been induced to invest their CPFIS in investment-linked products and unit trusts to obtain cash rebates for each transaction made without proper regard to the investment per se and the charges and fees which they have to bear, significantly depleting their CPF savings.

CPF has rightly taken steps to safeguard the first $20,000 in the Ordinary Account and the first $30,000 in the Special Account by not allowing these sums to be invested in CPFIS. CPF has also introduced CPF LIFE to ensure that those who retire in the future will have at least a certain amount for as long as they live. The amounts are certainly not enough for most retirees and must be supplemented by cash plans. Annuity products also ensure that there will be income for as long as the annuitant lives and are an essential part of retirement planning. Unfortunately, the "returns" of annuity plans today are not so attractive and many retirees have not invested in them. Reverse mortgage is an option to obtain cash and will likely become more popular.

The government's approach to defuse the retirement time bomb includes getting workers to work longer, getting children to maintain support of their parents, building lower cost housing for retirees and the Lease Buyback Scheme for HDB owners. The most effective long-term solution would be financial education so that Singaporeans would start financial planning early.

If, through this series of articles, we have contributed to raising the consciousness of the importance of financial planning and financial literacy of readers, we would count our efforts worthwhile. SL

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