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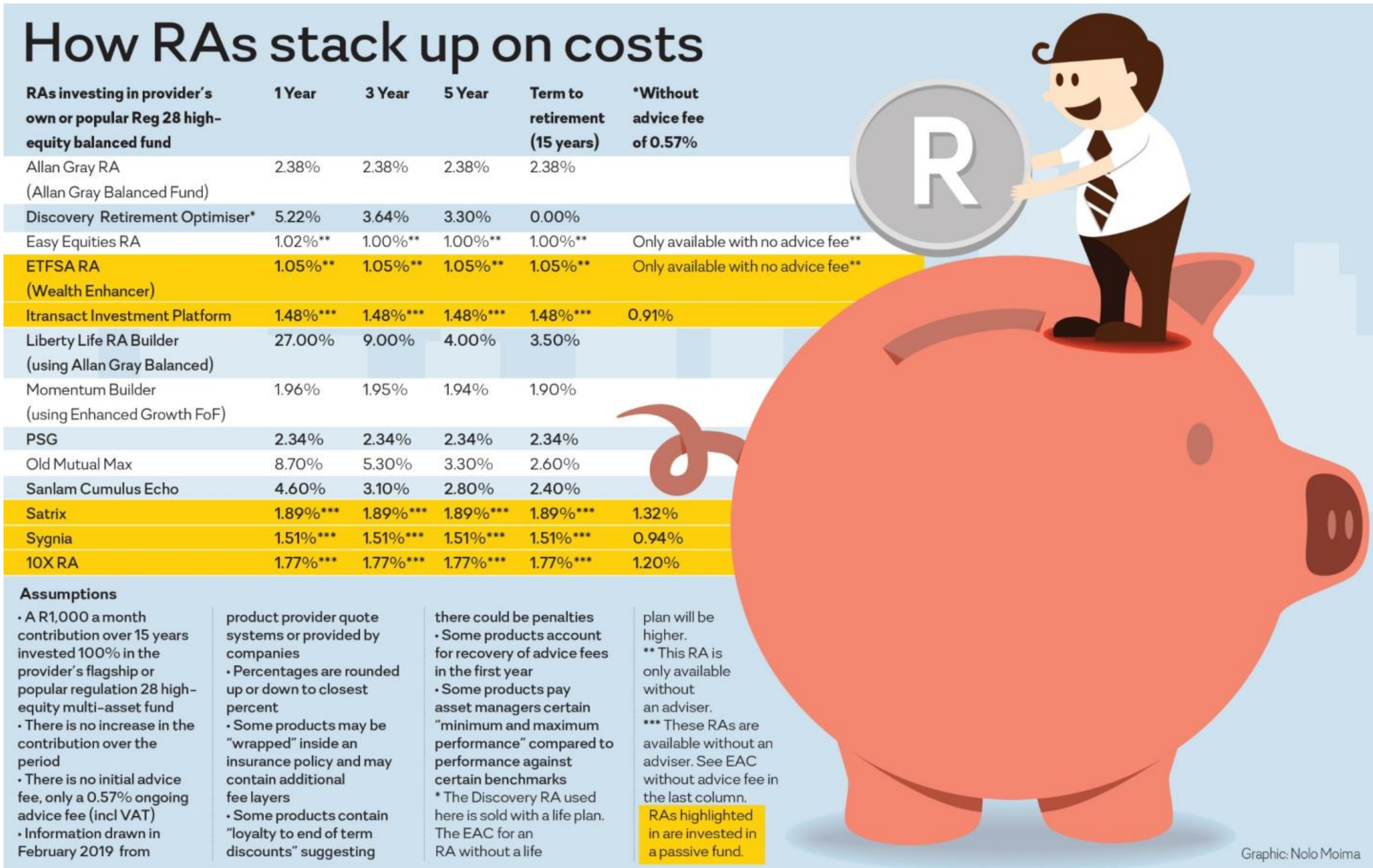
WHAT TO ASK WHEN CHOOSING A RETIREMENT ANNUITY

February is a good time to re-assess the tax savings you can achieve from contributing to a retirement fund.



How RAs stack up on costs

RAs investing in provider's own or popular Reg 28 high-equity balanced fund	1 Year	3 Year	5 Year	Term to retirement (15 years)	*Without advice fee of 0.57%
Allan Gray RA (Allan Gray Balanced Fund)	2.38%	2.38%	2.38%	2.38%	
Discovery Retirement Optimiser*	5.22%	3.64%	3.30%	0.00%	
Easy Equities RA	1.02%**	1.00%**	1.00%**	1.00%**	Only available with no advice fee**
ETFSA RA (Wealth Enhancer)	1.05%**	1.05%**	1.05%**	1.05%**	Only available with no advice fee**
Itransact Investment Platform	1.48%***	1.48%***	1.48%***	1.48%***	0.91%
Liberty Life RA Builder (using Allan Gray Balanced)	27.00%	9.00%	4.00%	3.50%	
Momentum Builder (using Enhanced Growth FoF)	1.96%	1.95%	1.94%	1.90%	
PSG	2.34%	2.34%	2.34%	2.34%	
Old Mutual Max	8.70%	5.30%	3.30%	2.60%	
Sanlam Cumulus Echo	4.60%	3.10%	2.80%	2.40%	
Satrix	1.89%***	1.89%***	1.89%***	1.89%***	1.32%
Sygnia	1.51%***	1.51%***	1.51%***	1.51%***	0.94%
10X RA	1.77%***	1.77%***	1.77%***	1.77%***	1.20%

Assumptions

- A R1,000 a month contribution over 15 years invested 100% in the provider's flagship or popular regulation 28 high-equity multi-asset fund
- There is no increase in the contribution over the period
- There is no initial advice fee, only a 0.57% ongoing advice fee (incl VAT)
- Information drawn in February 2019 from product provider quote systems or provided by companies
- Percentages are rounded up or down to closest percent
- Some products may be "wrapped" inside an insurance policy and may contain additional fee layers
- Some products contain "loyalty to end of term discounts" suggesting there could be penalties
- Some products account for recovery of advice fees in the first year
- Some products pay asset managers certain "minimum and maximum performance" compared to performance against certain benchmarks

* The Discovery RA used here is sold with a life plan. The EAC for an RA without a life plan will be higher.
** This RA is only available without an adviser.
*** These RAs are available without an adviser. See EAC without advice fee in the last column.

RAs highlighted in are invested in a passive fund.

Graphic: Nolo Moima

You may want to check whether you can save by topping up your retirement savings before the tax year ends on February 28, or after this week's budget you might want to check what you should contribute for the new tax year starting on March 1.

If you decide to contribute more to your retirement fund, and you are employed, you should begin by finding out whether you can contribute to your employer-sponsored fund as sometimes the fees are lower than on a fund you can access as an individual through a financial institution.

However, if you complement your employer-sponsored retirement savings or you are forced to save into a retirement annuity (RA) because you are self-employed, the choice of products is wide and confusing. Asking the right questions can help narrow the field.

Is it a policy with terms and penalties?
Is the RA "wrapped" as a life assurance policy with contractual terms that stipulate you must make

a regular contribution for a specified term with set increases each year where you could be penalised, or is it one without these constraints?

While a contract can help you be disciplined about saving, should some financial crisis arise - such as losing your job - breaking the contract by stopping or reducing your contributions could result in the life company imposing certain penalties.

You do not need to agree to the terms that come with some RAs, however. So-called new generation RAs offered by some investment platforms and unit trust companies have none of these terms, allowing you to sign up for a regular contribution but stop or reduce that contribution should you need to, at any time.

In the past, financial institutions have imposed stiff penalties of up to 30% of members' savings in RA policies for stopping or reducing contributions. Newer RA life assurance policies can only impose penalties of up to 15% of your savings although this should reduce each year until after 10 years when no penalty can be imposed.

Some RAs now offer loyalty bonuses that are paid if you stay invested for a certain period. Although it appears you won't be penalised if you need to reduce your contributions, you will typically pay higher ongoing costs to fund the loyalty bonus, says Wouter Fourie from Ascor Independent Wealth Managers. He is co-author of The Ultimate Guide to Retirement and a former winner of the Financial Planning Institute's Financial Planner of the Year award.

Steven Nathan, CEO of 10X, says there is no magic in the bonus. A policy like Sanlam's Cumulus Echo RA has high product and asset management fees - potentially more than 4% a year - and paying that entitles you to a boost on your savings after 20 or 30 years. But if you stop the RA early, you lose the money you could have saved had you paid low fees from the start, he says.

Lance Solms, head of the Itransact investment platform, says very few investors meet the requirements to earn the loyalty bonus because of changing life circumstances.

The RA offered by Discovery, for example, offers bonuses that depend on your use of other Discovery products, such as its credit card or life policy, and your initial investment.
Funds in an RA cannot be withdrawn until you reach age 55, and although you should keep contributing for as long as possible to enhance your income in retirement, you should not bind yourself to a contract that you may not be able to honour, if, for example, you lose your job.
Fourie says if you do sign up for an RA policy with a contractual term, take it to age 55 only.

What are the underlying investments?
Most new generation and life policy RAs offer an array of underlying investments.

Some new generation RAs only give you access to that provider's funds as investment choices. For example, if you invest in Satrix's RA you will only be able to choose Satrix funds. But investment platforms offered by the likes of Glacier by Sanlam, Old Mutual Wealth, Investec, Allan Gray, Momentum Wealth and PSG give you access to both their own funds as well as the funds of several other managers. Some RAs, like that from low-cost passive provider 10X, offer only a single investment portfolio.
You may be forgiven for thinking more choice is better, but your investments must always comply

with regulation 28 of the Pension Funds Act, which means the simplest choices are multi-asset funds that are regulation 28-compliant.

Nathan says you don't need a wide array of funds from which to choose - you just need to choose a good high-equity multi-asset or balanced fund that can hold up to 75% in equities and up to 30% offshore to ensure you enjoy good inflation-beating growth over the long term.

Investing in blue chip companies gives you the highest return over time relative to cash and bonds, but you are obliged to diversify across the asset classes when you invest in an RA and this will give you a smoother investment ride, Nathan says.

Fourie suggests diversifying across more than one multi-asset fund to reduce risk and volatility. Life assurers that offer a choice of underlying investments on their RAs typically include portfolios with guarantees and smoothed bonuses.

You should consider whether you really need these, especially if you have a long investment time horizon (a long time to retirement or a plan to fund your retirement income from investments) during which to ride out the market ups and downs, without guarantees or smoothing, as both incur additional costs.

Some RAs offer only passively-managed or index-tracking investments, some offer a combination of actively managed and passively managed and some offer only actively managed investments. Passive investments are cheaper than active funds, but your investments will return in line with the markets less costs, unless they track smart beta indices and are tilted towards certain shares that are expected to beat the market.

What is the asset allocation strategy?
A key difference between RA funds is how they allocate investments between the different asset classes.

The allocation between asset classes may never change (static), may change over the long term as the longer-term outlook for asset classes change (strategic), may change periodically (dynamic), or may be managed actively in line with market conditions and the manager's view on which asset classes will perform best (tactical).

The asset allocation strategy will impact the long-term performance of your fund, but the jury is out on which is the best method as returns from asset allocation calls are not disclosed separately from returns earned from stock selection.

Fourie says most of us are not equipped to decide which strategy is best. He suggests leaving these decisions to an expert multi-manager or the discretionary investment manager used by your adviser to manage investments for their clients.

Good multi-managers and discretionary investment managers have the skills to select the right combination of managers and to negotiate discounted fees to offset their additional costs, Fourie says.

Some RAs use life-staging, which means they lower your exposure to riskier asset classes (de-risk) as you approach your official retirement date. However, members who plan to transfer their investments from an RA into an investment-linked living annuity from which to draw an income in retirement, may not want to de-risk as they approach retirement. The asset allocation strategy, the performance of the underlying funds and the costs will all impact the amount you have at retirement.

The biggest contributors to disappointing outcomes at retirement are a failure to save consistently for long enough and a failure to understand the costs over time.

Rather start saving than let the complexity stop you from saving.

What are the costs?

When you ask about costs include all these fees:

1. Policy fee:
Most RAs will have a policy or administration fee to cover the costs of running the fund.

2. Platform fee:
RAs that offer access to different underlying unit trust funds are offered on an investment platform for which you will pay an administration fee. This fee may be charged on a sliding scale.

3. Investment management fees:
These are the fees on the underlying funds or portfolios that are charged as a percentage of the value of your savings. Some funds charge performance fees - a percentage of the amount by which your returns exceed a predetermined performance hurdle or benchmark.

4. Advice fees:
If you make use of the services of an adviser, your RA costs may include an ongoing advice fee agreed between you and your adviser.

5. Debit order fees:
Investing in some RAs through a regular debit order can also incur a debit order fee. Some providers subsidise this cost.

An effective way to measure all the costs is to compare the effective annual cost (EAC). You should demand an EAC when you obtain a quote. This allows investors to better understand the impact of fees and costs. You can use the EAC to determine how much you pay in fees, Lance Solms, director of Itransact, says. If your fund returns 10% before fees over five years and the EAC for five years is 2%, you are paying 20% of your return away each year in costs.