

## **Don't risk your members dying poor – encourage them to decumulate!**

Ever wondered what you'll be doing during retirement? Or where you'll be? A significant number of New Zealanders see themselves buying a caravan and travelling around the country, enjoying their new found freedom...but what if their planned retirement income is depleted before they hit the road?

Managing savings in the post retirement phase is a growing issue among New Zealanders, partly as a result of people living longer but also as a result of people's expectations regarding the quality of life in post retirement. Many New Zealanders haven't really considered how long they can expect to live and how much they will require in retirement savings to support themselves. Gone are the days when 75 years was a good age to reach.

In today's climate, New Zealand investors are focusing on market uncertainties and saving for retirement, but how many are thinking about how to manage their post-retirement incomes?

What exactly is decumulation? According to Steve Schubert, Director of Superannuation at Russell Investments, decumulation defines the phase in post retirement when superannuation investment is slowly withdrawn to provide a retirement income – the opposite to 'accumulation' where investors are saving for post retirement. Increasingly, the decumulation phase is becoming just as important as the accumulation phase of building up the retirement nest egg.

One of the challenges for superannuation funds is encouraging investors to save enough during the accumulation stage to live comfortably in retirement. Many people underestimate how long they will live by focusing too much on the average life expectancy of males and females. The average man will live to 76, whilst the average woman will live to 81. However information derived from Statistics New Zealand shows that of those who reach 65, more than one in two New Zealand women and more than one in three men may go on to live to 85. Furthermore, 11 per cent of women and 5 per cent of men may go on to reach 95.

Medical advances such as early detection of cancer, drug treatments and surgical procedures, along with sharp reductions in the number of female and male smokers, are prolonging life expectancy. This trend is expected to continue, with current international research suggesting that further increases in longevity remain possible.

How should superannuation funds assist with managing the risk of outliving one's savings? The first step is to understand it. This means recognising, and making members aware, that average life expectancy is increasing, and that there is a good chance that people will live longer than the average, possibly a lot longer. The second step is understanding the 10-30-60 rule which provides a guideline to managing and generating post retirement income. If an individual saves a constant percentage of pay from age 25 to 65 during the accumulation stage then decumulates for around 25 years, then the rule states that for every dollar of retirement income, 10 cents consists of savings during the accumulation stage, 30 cents comes from earnings off savings during the accumulation phase and 60 cents of retirement income comes from investment returns earned during the decumulation phase.

Super funds also need to develop products to assist with minimizing risk surrounding retirement income. For example, there is virtually no opportunity in New Zealand for investors to buy lifetime annuities when they retire.

We hope to see a greater variety of products available to investors in the future.

In the meantime, it is important that superannuation funds encourage investors to save enough during the accumulation phase and educate their members about the incentives available to them – from, for example, Government contributions, salary sacrifice or employer matching. Kiwisaver is playing an important role in this.

However, the need to accumulate wealth before retirement is only half the story. Investors should also focus on generating income for life after retirement and this is where the 10-30-60 rule comes into play. The bottom line is that no one knows exactly what age they will live to – the average New Zealander can only work with the known factors to influence the outcome – so besides accumulating, they need to quit smoking, exercise, and decumulate!

Steve Schubert is Director of Superannuation, at Russell Investments will be speaking on decumulation at the upcoming ASFONZ conference on 28<sup>th</sup> and 29<sup>th</sup> of August.

**Dr Edward Schuck, Managing Director, Russell Investments, New Zealand**