THE THREE COMPONENTS OF RETIREMENT PLANNING

THERE ARE THREE things you need to bear in mind when it comes to retirement planning — adequacy, sustainability and protection against inflation.

Private Pension Administrator Malaysia CEO Datuk Steve Ong tells *Personal Money* that retirement planning is a big concept, and it needs to be broken down into the three basic components so that people will know what to focus on.

ADEQUACY

"Adequacy is about replacing your earned income. Whatever salary you bring home buys you a certain standard of living that you've become accustomed to, and post-retirement, you need to replace that income with at least two thirds of your last-drawn pay," explains Ong.

Why two-thirds? Currently, one third of your income goes to deductions and work expenses. "Once you're retired, you no longer have tax or EPF deductions. Also, you won't have work-related expenses, which probably works out to another 20%. Two thirds of your last-drawn income will allow you to continue in the lifestyle you have become accustomed to."

How does one save enough to enjoy living on two-thirds of one's last-drawn pay during retirement? "You need to put away one-third of your current salary," says Ong.

The good news is Malaysia has a very successful mandatory savings scheme, the Employees Provident Fund. Under the scheme, the employee is required to contribute 11% and the employer 12%, which add up to a total of 23%. "If you have 23% salted away in the EPF, it means you're still lacking 10%, though that figure depends on your age. We've run the figures for someone who is 25, and it's 10%. If you're nearing 40, it would be closer to 15% to 20%.

"Say you put 10% into a fund that compounds your return at 6%, our numbers show that you have a good opportunity to enjoy two-thirds of your last-drawn pay [during retirement]," says Ong.

SUSTAINABILITY

Sustainability is linked to longevity. At the moment, says Ong, the current life expectancy for females is 76 and for males, it is 74. He thinks these figures are rather pessimistic. "The life expectancy of Singaporeans is already 82 and 80 for females and males, respectively. The average life expectancy for someone in Hong Kong is 84. So if you take a Hong Kong life tenure, you could easily be looking at 25 years of post-retirement," he says.

The EPF has pointed out that most people withdraw their money in a lump sum as soon as they're eligible and treat it as a windfall, rather than as their retirement funds that will have to carry them through the rest of their lives.

So, they blow it on trips around the world, a new car, paying for their children's weddings and the money is gone within three to five years. "The phrase is 'income replacement', which means you need income on a monthly basis. If you're talking about 20 years, that's 240 months of consistent withdrawals for you to continue to enjoy the life you have been accustomed to," says Ong.

What most people do is transfer their money out of the EPF into a bank account, which Ong points out, means an immediate loss of income. "The EPF pays you 6% while your fixed deposit will pay you about 3%, so immediately

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you have a shortfall."

The solution, he adds, is to transfer your money into a retirement money management account. "The Private Retirement Scheme (PRS) is designed for money management. If you have been saving diligently, putting away 10% into your PRS account, upon retirement, you then tell your fund manager, now I'm in retirement mode, we would need to manage risk by switching to a more income-generating fund.

"And you ask your fund manager to get you into a fund that give you returns exceeding the inflation rate so that your standard of living is not affected by rising inflation. You tell your fund manager that you need the money to last for at least 25 years and tell him to transfer RM5,000 (or whatever your amount is) to your bank account every month. That's what the PRS can do for you. And that's what all retirees will need to do," Ong points out.

PROTECTION AGAINST INFLATION

And the last thing to do is ensure that the fund you invest in is inflation-adjusted. "Retirement planning sounds like a big problem but by breaking it down into bite-sized chunks, you have a way to avoid the problem," says Ong.

His advice? Save as much as you can for your retirement. "You can stinge on food, you can stinge on clothes, but don't stinge on your retirement savings. And do not, on any account, take money out of your retirement fund to pay for other expenses.

"It is not a source of cash; if you want to travel, go out and earn more money or save towards it. If you want to pay for your children's education, save under an education fund. When you don't have a dedicated retirement account, what you have is a general deposit account that you use for everything. And when it comes to retirement, how much do you have left? You don't know."

What about those who are approaching retirement? "Last year, when we did 30 public seminars, half of the people who attended were pre-retirees and retirees. For retirees, we taught them about disciplined draw down of income. There's not a lot of magic surrounding this. How much money do you have in the bank? We can help you put it in a relatively low-risk, income-generating fund.

"If you're late in the game, at least we can still advise you so you don't continue to be ignorant about it and leave it all the chance," Ong says.

Two years ago, there was no PRS scheme in Malaysia. Now, he says, Malaysia has two pillars of retirement – the EPF and the PRS. "If we secure these two pillars, it won't matter if the rest of your investments go wrong, because it won't affect your financial security." ***By Jennifer Jacobs***