Assuming you're planning to clock out of the workforce at around age 65 the difference between a no-frills existence – courtesy of national super – and some degree of comfort – depends on how much you've managed to save. Most people struggle to save much at all – so what's your strategy?

Beating the retirement blues

By Mark Story

At face value the results from the annual Sovereign SaverPulse Survey of savings and investment attitudes makes little sense. Instead of providing meaningful insights into savers' underlying thinking the survey result shows unrealistic amounts of optimism, an errant breakdown in logic, and an alarming indifference towards saving.

Nevertheless, expectations of having enough savings to support them in retirement - even though "state-funded" superannuation and inheritance booty are now perceived (by most) as problematic at best - remain high. While 78% of people don't believe the Government will provide them with an adequate retirement income, these same people are not making plans on how to supplement their superannuation either.

Family home

So what's their secret? All fingers, so the survey suggests point to property. Many who haven't started saving for their retirement see the family home as a surrogate retirement asset. In fact, of the two thirds of those savers sampled, 33% see their home as an important part of their retirement savings plan. Not surprisingly, 23% believe residential property investments delivers the best return – over double that of any other type of investment.

Considering the inconsistency within NZ's investment tax laws, coupled with ambiguity shrouding most superannuation schemes, Simon Swanson, managing director with Sovereign believes NZ's unique investor psyche – reflected in a preoccupation with property - is perfectly logical. In a perfect world, he agrees investors would be better served retiring mortgage and credit card debt than scattering lumps sum between various fixed interest accounts. It's a no-brainer really, why would any sane investor keep money in a term deposit earning 3.5% when they're paying 7% on their mortgage?

Clearing the mortgage
Admittedly, having all your assets in the family home is inconsistent with portfolio investment principles. But going all out to pay off the mortgage by the age of 45, then keeping up the same payments into financial assets is a strategy few will argue with. The trouble, says Swanson is too many investors favour a false sense of savings security over more practical wealth creation strategies. "The fact that most investors don't do it or are too interested in living for today suggests contractual savings are the only way of getting people to save for retirement."

Interestingly enough, survey results indicate that investor sentiment – which unanimously rejected the ill-fated Winston Peters-led referendum into compulsory superannuation - has gone 180 degrees. In fact, a whopping 71% favour some form of compulsory savings scheme, while 67% said they would participate in an employer-based retirement scheme (if offered one).

Most (52% of people surveyed) admit to not having started saving for their retirement.

Cry for help
The lead that current investment regulations has put in the saddle-bags of those wanting to save for retirement has forced many to side-step superannuation schemes and take a D.I.Y approach. But what survey results prove convincingly, argues Swanson is that a D.I.Y approach to retirement savings is beyond the capability of many investors.

What's warmed investors to compulsory superannuation, suspects Swanson is an admission that when it comes to saving, many investors are crying for help. There's no clearer evidence of investors' clarion call for savings guidance than 40% of SaverPulse respondents who admit to finding it difficult to decide on saving and investment decisions.

With fewer than 30% of people surveyed using a financial planner, it's hardly surprising that only 32% of the total were very confident they were making the right investment decisions. To Swanson, survey results are as close to an admission as we're likely to get that NZ simply got the answer to the compulsory superannuation question wrong. There's little doubt that compulsion will deliver the desired savings outcomes. Like most people, he'd like to see a private-sector solution. But assuming there's something in the local psyche that invalidates the proposition - that Kiwis' can save without some hand-holding - he has no problem with the compulsory approach.

Scare tactics

There's clearly no carrot to encourage saving for retirement. But financial advisor Murray Weatherston claims soothsayers of the "big stick" theory – namely that there'll be no state-funded super for future generations - have gone too far. He believes financial advisers who frighten investors into saving for retirement with this rhetoric are blatantly irresponsible.

Weatherston reminds investors that political debate surrounding "national super" is less around 'if' and more about 'when' you'll get your hands on it. "If you're under 50 today, you may indeed have to wait a little longer (say 68) to get 65% of the (ordinary time) average wage," says Weatherston director of Financial Focus. "Given the level of 'NZ super' - $19,600 for a married couple - it's irrational for Kiwis to save anything."

Limited savings

People typically have the capacity to save most in their 20s when they're single or in their late 40s when most of the mortgage is paid off. But most parents, argues Weatherston don't have a spare $20,000 to save annually, while many households just don't have the capacity to save much at all. "If you need your current income to live on, saving is likely to be the last thing on your mind."

Favourable tax incentives, says Weatherston will go some way to staunching NZ's dwindling investment climate, fashioned by too much consumption and too little savings. Earnings from savings invested through superannuation funds, life offices and similar entities - currently taxed at 33c in the dollar - is a major disincentive to save for those on lower marginal tax rates (people earning under $38,000).

Not surprisingly, the SaverPulse survey suggests things are getting worse, not

“If you need your current income to live on, saving is likely to be the last thing on your mind.”

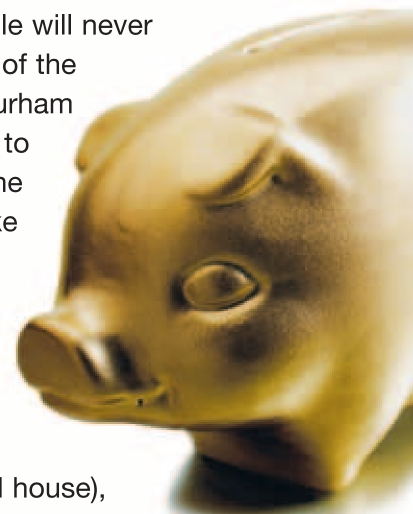
better. In fact, the number of people who claim to have started saving for retirement has dropped 5% in just 12 months. Adding insult to injury, the gulf between saving and consumption is widening. Number crunching by the Reserve Bank shows that for the year ending March the average household spent 11% more than its income (compared to -3% two years ago).

Eat your home

There are no brownie points for figuring out the net affect of low personal savings. With the average retirement income in the 65-69 age group only around $13,200, most people – despite SaverPulse survey expectations to the contrary - will have to rely on ‘NZ Super’ as their main or only source of retirement income. Assuming investors own their own home, ‘national super’ will at best provide for the very basics. Nevertheless, Irene Durham financial planner with Rutherford Rede says people in their 50s appear to be less reluctant to use the equity in their homes than they may have in the past.

What she’s witnessing is a growing interest in reverse annuity mortgages (RAMs) – a specially designed product that lets senior homeowners access the equity tied up in their home. Available to homeowners 65 years upwards, a RAM consists of two parts - a mortgage over the security property, and an annuity policy that secures the benefits advanced under the mortgage.

What a Ram does is provide an immediate and ongoing monthly income stream, plus retention of ownership and occupancy rights. RAMs also provide the assurance that the amount which is repayable will never exceed the fair market value of the property. Not surprisingly, Durham expects the uptake of RAMs to increase proportionately to the number of offerings that make their way to the market.



Selling the home

But with the average couple entering retirement with little more than $37,500 worth of financial assets (and freehold house), he says maintaining their standard of living may depend on whether they’re prepared to sell their family home.

Releasing equity in the family home and moving to the provinces can be an excellent retirement strategy, especially if you’re in a main centre. But Aaron Hing investment advisor with Spicers questions how profitable this strategy will be in 15 years if there’s an entire generation of baby-boomers flooding housing markets like Auckland with expensive homes.

Enough to retire on

So how do you work out how much you'll need to retire on? In answering this question, Hing prefers to work backwards by asking: When you retire how much do you want to spend, and how much you expect the Government to contribute?

The remainder is how much you'll need to chip-in to reach your target. It's a useful exercise on many fronts, but what it usually does, advises Hing is realigns investors' expectations.

For example, how much of a lump sum would someone need to have saved to live on 70% of a modest wage - of say $50,000 annually (taxed amount $28,000)? Based on Hing's numbers, to generate a real rate of return of 3.5% an investor (at say 65) would need $490,000 in cash – which based on a combinations of principle and interest – would be extinguished at age 90.

Conversely, if the investor wanted to preserve the principle, they'd need around $800,000 in cash on retirement.

Regular contributions

Based on the difficulty past (and present) generations have with saving, most people won't have anything near this amount when they retire. This reality-

check, plus the level at which 'NZ super' is paid explains why financial advisers struggle to get people to take saving for retirement seriously.

This also explains in part, suspects Weatherston why financial advisers have become more preoccupied with clients who have lump sums than those wanting to save incrementally. "Many of my colleagues in the investing community don't like the idea of the regular contributions business – that's what insurance salesmen used to do."

When you retire how much do you want to spend, and how much you expect the Government to contribute?

Instead of ploughing all their savings into the family home Weatherston advises his clients to spread their exposure to different markets. He recommends investors pay down the mortgage to a level they're comfortable with then get exposure to financial assets with long-term growth potential.

That means finding an investment advisor who's as capable with the lump sum as regular contribution business.