SA's two-pot retirement system shines light on the need for supplementary savings plans

With the imminent implementation of the National Treasury's two-pot retirement system, the urgency for supplementary savings plans has come to the forefront. These plans play a crucial role in securing a financially stable retirement for South Africans.

Source: https://www.pexels.com/search/savings/Pexels

The new system, proposed to come into effect in March 2025, will divide contributions into two clear categories: two-thirds will go towards mandatory retirement savings, while one-third will be designated for a savings pot, offering the option of annual withdrawals to help with unforeseen financial challenges.

Keith Peter, advice manager at Old Mutual Personal Finance, notes that while early access to retirement savings will provide short-term relief to financially stressed South African families and individuals, it is not a permanent solution to obtaining financial freedom.

He says, “We understand the pressures many people face in the current economic environment, yet we must also consider our financial future. Accessing retirement savings can be a vital first step to financial recovery, but relying on long-term investments to solve immediate financial distress is not a permanent solution.”

He says the prudent course of action for individuals and families is to work towards setting up supplementary savings plans

– a financial strategy that augments primary savings or retirement funds – that can minimise the need to access retirement savings regularly and top up any anticipated shortfalls in retirement.

“Obtaining financial freedom and reaching your goals usually demands self-control and patience. Finding a balance between saving for the future and enjoying your current life is critical,” he says.

Below, Peter notes the guidelines consumers must consider when employing a supplementary savings plan.

- ## Consult a financial adviser

Consulting a financial adviser is crucial when considering supplementary savings plans tailored to your unique financial situation and goals. An adviser will provide insights into the impact of regular withdrawals from the savings pot, offer guidance on fund selection to align with individual retirement objectives, and consider factors such as age and income.

Additionally, they can help explore options like voluntary investments, which can serve as an emergency fund to prevent premature withdrawals and allow pre-retirement capital to grow untouched.

Peter says, “These investments can also supplement retirement savings, addressing limitations in existing retirement funds or tax deductibility issues, provided extra funds are available for investment.”

Advisers can also guide individuals on budgeting to help manage and allocate resources effectively, ensuring the means to pursue supplementary savings and other financial goals.

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- ## Draw up and review the budget

Peter urges savers to regularly review their budgets and financial goals to ensure consistent progress towards securing their retirement future. This would include adjusting spending habits and savings contributions to align with retirement objectives.

Peter says that effective budgeting and financial planning are indispensable for maintaining financial stability while safeguarding retirement dreams.

He says, “Keep yourself informed about changes in the retirement landscape and tax regulations. Understanding the nuances of the two-pot retirement system empowers you to make informed decisions. Staying updated on industry developments and financial news lets you finetune your financial strategy, ensuring your retirement goals remain on course.”

- ## Set up an emergency fund

For those who have the means, Peter says, a vital step should be a rainy-day fund, a dedicated savings account or a pool of money to cover unexpected or unplanned expenses.

Peter says, “Building up an entirely separate nest egg for emergencies for unforeseen expenses rather than dipping into the savings pot will cover any unexpected or unplanned expenses. These expenses can include medical emergencies, car repairs, job loss, home repairs, or any other unforeseen financial challenges that may arise in life.”

He says this fund will provide a financial safety net, allowing individuals or households to address these unexpected costs without resorting to high-interest debt or depleting their long-term savings or investments.

- ## Choose the best savings option

When you are ready to save more, alternative retirement savings options, such as tax-free savings accounts, offer tax advantages and allow disciplined savers to withdraw funds to supplement their retirement.

Endowment products, investment schemes with a contractual maturity date, provide another path to disciplined savings, though access is limited in the first five years. Remember, endowments are subject to tax.

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20 Oct 2023

- ## Prioritise the suitable investment for the right time

The two-pot retirement system maintains a fixed 1/3 and 2/3 contribution split for retirement funds, which may not account for individual circumstances. Factors like income, age, and financial goals can influence contribution targets.

Tax considerations are pivotal, allowing contributions of up to 27.5% of taxable income or remuneration, capped at R350,000 annually. If one's retirement objectives demand contributions exceeding this limit, prioritising savings over the annual tax deduction is advisable, with the excess contributions carried forward to the following year to reduce your tax.

Assessing whether these funds are invested conservatively, moderately, or aggressively is crucial in determining long-term capital growth potential. Age also plays a role; younger individuals can adopt more aggressive investment strategies due to longer time horizons and greater market resilience.

Transitioning to conservative investments is recommended to safeguard accumulated capital around five years before retirement.

- ## Regularly reassess your financial objectives

To protect retirement goals, reassess financial objectives and consult a financial adviser. Imagine aiming for a post-retirement income of R10,000 per month, requiring R2m in savings by age 60. However, repeated withdrawals may leave individuals short of their target.

“To address this gap, optimise your investment strategy; engage with your financial adviser to review the investment options in your pension, provident, or Retirement Annuity (RA) fund,” he says.

“Integrating these considerations into the overall financial plan is paramount. Collaborate closely with your adviser to finetune your strategy. Determine whether risk tolerance aligns with the proposed investment adjustments,” Peter concludes.