Social security and retirement funding: Perspectives from the Financial Diaries

Daryl Collins

September 2007

WORKING DRAFT

CONTENTS

1. INTRODUCTION

At the centre of most low-income households' retirement funding is the old age grant provided by government. This benefit supports not only recipients but also their families. But is it enough to allow households to maintain living standards are they move into retirement? Is it really the only means that the elderly have to support themselves, or are there other resources? Does the expectation of the old age grant crowd out personal savings among young adults? How do those whose incomes are above the means test for old age grants, rendering them ineligible, save for retirement? How effectively are low-income South Africans preparing themselves for retirement?

The Financial Diaries, which tracked the intricate details of money-management in poor households over a year, provides some insight into these questions. The Financial Diaries dataset was used to investigate both individuals who have retired and others of working age. For those who have retired, how has savings funded the income needs of households? For those that have yet to retire, how many have long-term savings that may ultimately be used for retirement? These questions are analysed both in terms of stocks, the overall assets a household has built, and flows, and how households accumulate these funds. The sources of retirement support are considered in the context of the categories developed by the World Bank for describing different forms of retirement provision[1]:

> **Pillar Zero**. Social security or social assistance programme run by the government, such as the old age grant.
>
> **Pillar One**. A social security or social assistance programme supported by compulsory contributions of working citizens. This does not exist in South Africa.
>
> **Pillar Two**. A mandatory saving system, usually managed by the private sector or in partnership with government entities, compelling citizens to save for retirement. This also does not exist in South Africa.
>
> **Pillar Three**. Supplementary pension accumulation, which is not mandatory but usually attracts tax subsidies. There are numerous examples of these types of plans in South Africa.
>
> **Pillar Four**. Captures all forms of old age provision or support not included in any of the other pillars, including family or community support.

This report is in six sections. Section 2 explains the Financial Diaries data set and describes the different ranges of income it covers. Section 3 looks at the retirement support being accessed by people in the Financial Diaries who have retired. Section 4 uses some of the lessons learned from Section 3 to assess how prepared adult households are for retirement. Section 5 discusses two specific policy ideas. Section 6 deals with the conclusions.

---

[1] World Bank (2005) *Old Age Income Support in the Twenty-first Century: An International Perspective on Pension Systems and Reform*, written by a World Bank team lead by Robert Holzmann and Richard Hinz, February 2005.

The key findings for retirees and pre-retirements adults are summarised below.

For retirees

- Retired people fall into two categories: those who rely on government old age grants and those who rely on monthly pension payouts. Those who rely on old age grants, with an income per capita of only one fourth of those reliant on pensions, are by far the worse off of the two groups.

- Regular monthly payments contribute more to retirement support than lump sum payments from retirement annuities, assets sales or other financial savings. Lump sum payments tend to be diverted to uses for other family members, such as initiations, schooling and funerals.

- Pillar Four sources of retirement support were observed, but they are not the primary sources of support.

For pre-retirement adults

- Bank accounts and *stokvels* are the main ways that households save out of cash flow but this saving tends to be geared toward short-term goals rather than retirement.

- Assuming all savings flows, financial and physical assets are used for retirement, 70% of adult singles and married couples would have more than five years of retirement support at the time of retirement. If physical assets are excluded, 46% of adult singles and 53% of married couples would have more than five years of retirement support at the time of retirement.

- A more realistic scenario would exclude all physical assets and savings flows going into bank accounts and *stokvels*. Under this scenario, only 15% of adult singles and 18% of married couples would have more than five years of retirement support by the time they retired. In short, with the exception of employer-provided provident and pension plans, most low-income South Africans depend on the state-provided old age grant for support in their old age.

2. FINANCIAL DIARIES DATA

The Financial Diaries dataset[2] was constructed to examine a variety of questions about financial management in poor South African households. Detailed daily income, expenditure and financial transactions were captured over the course of a year by means of a fortnightly interview. The emphasis in the Financial Diaries study is on understanding poor households at a detailed level rather than using a broad sample to make conclusions about the South African population.

Given that most poor households in South Africa are black, the sample focused on 152[3] black households in the following areas: Langa, Cape Town (urban); Diepsloot, Johannesburg (peri-urban); and Lugangeni, Eastern Cape (rural). With the intention of examining diversity in households within those areas, the sample is also drawn across different dwelling types and wealth levels.[4] A combination of qualitative and quantitative data was collected. The compilation of detailed household cash flows was accomplished over 13 months from November 2003 to December 2004. Table 1 shows the sample across areas and uses the common global poverty lines of $1 and $2 per person per day to demonstrate the levels of poverty in each area. In the urban areas, very few of the households could be considered extremely poor, whereas in the rural area about 22% of the sample lives on less than $2 per person per day.

Table 1: Financial Diaries sample, percent of households, by dollar-a-day income

	Diepsloot (Urban)	Langa (Urban)	Lugangeni (Rural)
Above $10	39%	40%	19%
$5 - $10	29%	33%	22%
$3 - $5	12%	18%	17%
$2 - $3	16%	9%	19%
$1 - $2	4%	0%	17%
Below $1	0%	0%	5%

[2] The Financial Diaries is a research project based at the University of Cape Town and funded by the Ford Foundation, FinMark Trust and the Micro Finance Regulatory Council of South Africa. See www.financialdiaries.com for more information.

[3] The sample started out with 181 households and had an attrition rate of 19% through the survey year. The analysis shown in this paper is based on the 152 households for which we have a complete set of data.

[4] Collins, D. (2005) *Financial instruments of the poor: Initial findings from the Financial Diaries study*. *Development Southern Africa*, 22(5): 717-28.

3. INCOME SOURCES FOR HOUSEHOLDS WITH RETIRED PEOPLE

It is useful in describing the financial management practices of the poor to distinguish between regular, monthly income flows and lump sums that appear from time to time. Economic research suggests that means and frequency of income allow people to create "mental accounts", a system under which they tend to designate certain streams of income to pay for different items.[5] Regular income streams may pay for regular expenditures such as food, while irregular streams of income may pay for a large asset purchase or an event such as a feast. Regular monthly flows would include the state old age grant and monthly pension payments, while lump sum payouts would include payments from retirement annuities, savings instruments, asset sales or irregular forms of support.

Monthly income flows

In the Financial Diaries sample, the urban areas of Diepsloot and Langa have very few households with older members, while rural Lugangeni has a very large percentage of households with elderly occupants. In the urban areas, the old age grant is extremely important to incomes of households with retirees, but other sources of income, coming from other households members, like wages, play more of a role than they do in Lugangeni. In Langa, two of these retirees are still extremely economically active. One of the retired people, 67 at the time of the study, is an undertaker and the entire family income (his and his son's) is earned from this business (his son works for him). Another retired person, who was 79 at the time of the study, works as a caretaker for a block of flats and receives a monthly pension from his previous job (two other sons worked casually but did not earn as much as their father). The other three retirees in Langa live primarily off the old age grant.

Table 2: Sources of income for households with members aged 65 and older

	Langa	Lugangeni	Diepsloot
% of households with members over 65	10.4%	41.4%	2.0%
Of those, % whose main source of income is from:			
Regular income from another member	20%	0%	100%
Old age grant	60%	75%	0%
Pension	0%	13%	0%
Other grants	0%	4%	0%
Remittances	0%	4%	0%
Business	20%	0%	0%

In Diepsloot, there was only one person, a 91-year-old man, who came to live with one of the households briefly. He lived primarily off an old age grant, although the other people in the house were working and also likely supported him. This was a short-lived situation (he went to live with another relative) and there were no other examples of any household member above

[5] See, for example, Thaler, Richard H. *Mental Accountng Matters. Journal of Behavioral Decision Making* 12(3), (1999): 183- 206.

the age of 65 in the Diepsloot sample. There is one other woman, aged 61, who does receive the old age grant in Diepsloot. However, given the sparseness of data, Diepsloot was not included in Table 2. In Lugangeni, the old age grant is clearly the dominant source of income, with monthly pension payments playing an important role in three of the twenty-four households with retirees in them.

If we look deeper into this sample, we can begin to group retirees into two categories. One group depends on the old age grant, and they have a very low income per capita. The other group depends on regular pension payments. They have a relatively high income per capita and are often a key source of financial support for their families.

Group 1: Dependent on the old age grant

Households with an old age grant recipient make up 50% of the households in Lugangeni, but only 8% of households in Langa.[6] For most of those in Lugangeni and Langa, this is the household's main source of income. Note that income per capita (R567 and R623 respectively) for these households is far less than the amount of the old age grant, which implies that these grants are being heavily used to support others in the household. For those with old age grants, over half of their monthly income comes from this grant.

Table 3: Households with old age grant recipients

	Langa	Lugangeni
Percent of sample	8.3%	50%
Percent of sample for whom this is the main source of income	6.3%	36%
Household monthly income per capita	567	623
Percent of income from:		
Old age grant	57.9	65.6
Other grants in household	0	9.1
Remittances	17.4	10.2
Wage income (from another member)	12.1	3.3
Pension (from another member)	5.2	8.9

Mamngwevu[*] is an example of a typical rural grant recipient. She is a 73-year-old widow who stays with her 50-year-old son, 23-year-old grandson and 12-year-old grandson. Neither of the adult men work, and the older one causes her a great deal of trouble. He expects to live off her old age grant (which was R740 a month at the time of the study) and the income from four school children who rent rooms from her at R60 each a month. He often asks her for money for cigarettes and liquor. She has another son who lives elsewhere and is working, who tries to give

[6] We looked carefully at whether there were households that should have received the old age grant, but did not or those that receive the old age grant but did not qualify for it. In the entire sample of 35 people who qualified for the old age grant on the basis of age and income, only two were not receiving it. One was receiving UIF and could have qualified for a partial old age grant and the other was a Zimbabwean refugee who did not qualify. Of the sample of 31 people who were receiving the old age grant, only two should not have qualified, being a few years too young.

[*] Names of respondents have been changed to protect their identity.

her money. She has another grandson who is also a problem – he was in a fight in which two people were beaten to death and is wanted by the police. Often during the year, she worried about money. Twice she was concerned about having enough money to go to the doctor.

A significant part of Mamngwevu's financial portfolio is in credit instruments – though she does have a bank account, a burial society and a *stokvel*. During the year, she had credit from two informal sellers, credit at three local spaza shops, a *mashonisa* (moneylender) loan, loans from five people and she took back-to-back loans from *stokvels* twelve times. Clearly, she has a difficult time managing her cash flow and she uses credit to augment her income and expenditure patterns. She has a very high debt service ratio[7] of 48%, one of the highest in the Financial Diaries sample. Many grant recipients have higher debt-to-income ratios than the rest of the sample and this indebtedness seemed to be more ingrained in the financial portfolios of grant recipients than those who are working.[8] This reflects not only the better access that grant recipients may have to informal debt, as opposed to, for example, someone who only relies on irregular income such as piecework or a small business, but also the low per capita income that these grant-dependent households have, which makes it difficult to make ends meet.

How well do these households cope when an emergency hits? During the Financial Diaries year, we witnessed one example of a grant recipient who was able to leverage her credit resources effectively when she needed to. Mapeyi[*] is a 72-year-old woman who came to Langa when she was a young woman with her parents, and later inheriting their house. Her three grandchildren live with her. All four members of this household are supported by Mapeyi's old age grant. Every now and then she makes ginger beer to sell, but this is not a consistent business. The mother of two of the children works in a nearby factory and lives elsewhere in the township. She does not contribute to the children's upkeep. The other child lost her mother during the study year, and her father had died when she was four-months old.

When this child's mother (she was Mapeyi's daughter-in-law) died, Mapeyi needed to help pay for the funeral. She borrowed R1 000[9] from the local spaza shop, from whom she used to take groceries on credit every month. The shop owner says that she rarely gives credit to anyone without a salary but Mapeyi is a special case because she's been in the neighbourhood so long and the shop owner knows she'll pay. She does, however, restrict the credit given to Mapeyi every month to R200 because she worries Mapeyi can't afford more. When she borrowed the R1 000, Mapeyi stopped taking groceries on credit, because she wanted to pay back the loan first. She did not pay any interest for either the loan or the credit.

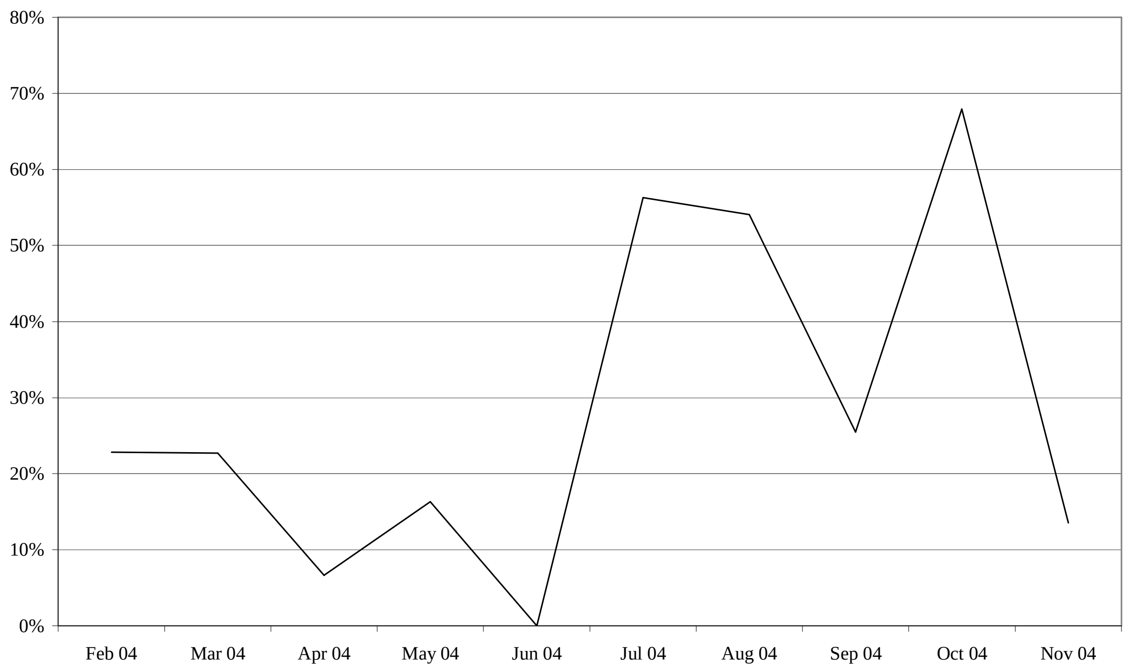
---

[7] The debt service ratio is the ratio of the sum of monthly payments towards all debt in the household, including informal debt, over the sum of all income in the household, including informal income, grants and remittances.
[8] For more details, see Collins (2007) *Debt and Household Finance: Evidence from the Financial Diaries*, *Development Southern Africa*, forthcoming.
[*] Names have been changed.
[9] In US$, this would be equivalent to $154, using an exchange rate of R6.5/US$1, which was the average exchange rate during the time of the study.

Chart 1 tracks Mapeyi's debt-to-income ratio as she took and then paid back this credit. Prior to borrowing the money in June, Mapeyi would manage her credit fairly tightly, paying back 10% to 20% of her income to the spaza. From June until October, while she was paying back the loan, she used between 30% and 60% of her income to pay the loan and restricted the household expenditures. She finished paying back the loan in October.

When we left Mapeyi at the end of the study, she was joining a burial society because she was concerned about her experience with her daughter-in-law's funeral. She says that she has a hard time keeping money aside and doesn't want the grandchildren to have that burden. She also applied for a foster care grant for the child who recently lost her mother. The social worker had come to see her and she was hopeful that the financial situation of the household would improve.

Chart 1: Mapeyi's debt payments as a percentage of income



Group II: Dependent on pension payments

A completely different group of retirees are pension recipients. Again, in Lugangeni there are more households who depend on private pension income than in the urban areas. These are people who have lived in urban areas or who have worked in public sector jobs as nurses or teachers and then returned to the rural areas to retire. In this sample, these pension payments are substantial and little other income is necessary to sustain the households, so pension payments count for a larger portion of total income than other sources. Pension recipients have a great deal more money at their disposal every month than grant recipients. In Langa, these pension payments are shared among a larger number of household members, so income per capita is still quite low on average. In Lugangeni, however, pension recipients are the most affluent in the community – income per capita in these households is four times what it is in grant-dependent households. This is partly because they earn more money, but also because they have fewer members in their households—an average of two compared to an average of four for all of Lugangeni. That said, they often provide the financial backbone for their extended family circle, contributing heavily for education and special events. They are also sophisticated financial managers and often hold private retirement annuities, which provide handy lump sum payments as well as their monthly pension check.

Table 4: Households with private pension recipients

	Langa	Lugangeni	Diepsloot
Percent of sample	6.3%	12%	0
Percent of sample for whom this is the main source of income	0.0%	7%	0
Household monthly income per capita	635	1863	-
Percent of income from:			
Pension	17.1	50.4	0
Grants	24.9	22.3	0
Remittances	10.4	14.4	0
Wage income (from another member)	33.2	11.1	0
Business	0.4	0.9	0

Nomtholo[*] is a good example of someone who lives off a regular monthly pension payment. She is a 61-year-old retired woman who lives with her 31-year-old unemployed niece in a big house in Lugangeni. She earned all her life as a nurse and managed her money exceptionally well. We calculated her net worth to be about R1-million. She holds R400 000 in a unit trust, and the rest in real estate. She has a large and newly renovated home in Lugangeni, as well as a house in Umtata. During the year, she sold her house in Umtata for about R150 000 and has kept the money in her bank account.

She receives two pensions every month – one from her work and one as the spouse of her deceased husband. Together they add up to about R7 000 a month. She also receives remittances from her daughter but these are forced. Every month she asks to "borrow" money and then she gives it back to her daughter when she needs it. She found that she was bored not working, so she started working as a nurse again on a six-month contract, where she earns R2 244 a month.

She has a vast array of financial instruments. She belongs to several formal burial societies and funeral plans to cover both her funeral and those of her children and grandchildren. She has credit accounts for the furniture in her new house. She has two bank accounts and a unit trust. She also has life insurance, as well as car and vehicle insurance. She has held retirement annuities that have paid out and supported both her home building and the education of her grandchildren.

Her wealth provides a backstop for many of her extended family. During the study year, she contributed R6 000 towards relative's funerals and traditional feasts. In addition, she gave

[*] Names of respondents have been changed to protect their identity.

roughly R15 000 in goods or cash to her children over the course of the study year, to cover a variety of needs such as paying the family of a women her son made pregnant but didn't marry; paying for the school and medical needs of a grandson who has cerebral palsy; and paying for the clothing of grandchildren.

Lump sums: Financial and asset-based income used for retirement

Monthly retirement income provides the core support for retired households, but irregularly-timed lump sums from other investments, like retirement annuities, or drawing down savings in a bank, or selling assets, may also be an important part of household survival strategies during retirement. How much are households using their previous investments (other than regularly received pension or provident fund payouts) for their retirement? What about the money saved in the bank, or livestock bought or inherited?

Financial savings

Financial savings did not feature significantly in the support of retirees. There are good reasons not to be optimistic about how much bank or *stokvel* savings can be counted on for retirement purposes. Oftentimes those savings were used for purposes other than support of the retirees themselves. On net, taking deposits into bank accounts less withdrawals from bank accounts, we do not observe much drawing down of financial savings to support retirement. Of the 24 people who were retired in Lugangeni, only 10 had bank accounts. None of them were pulling down assets on a regular basis – deposits every month were higher than withdrawals. We found a similar situation among the retired people in Langa and Diepsloot.

We observed only three retirement annuity payouts during the study year, and two out of those three were used for the benefit of other family members and not the retiree. One household used a payout of R1 800 to pay her daughter's doctor bills. Another decided to reinvest a payout of R20 000 to use for her grandchildren's education. Only the last used the payout for herself. She received R15 000 and used it to repair a car and start a transportation business.

Two rather sophisticated investments are worth noting. It took several interviews to understand that that Mzwamadoda* had a 32-day notice account. He is a 56-year-old man who lives in Lugangeni with his wife, Tembisa, one child and six grandchildren. They manage to get by month-to-month on two disability grants (R740 a month each at the time of the study). Mzwamadoda and his wife manage their day-to-day income and expenditures frugally. They have two *stokvels*, primarily used for school fees and Christmas. They also belong to several burial societies to help with funeral expenses should they or any of their children pass away.

When Mzwamadoda was retrenched in 2001, he received a lump sum retrenchment package of R200 000. From this, he bought five cattle (which he still has) and one horse, and, on the advice of his former manager, he put the remainder (R190 000) into a Standard Bank 32-day notice account. With relatively high interest rates in the early years, he enjoyed an interest income of about R1 000 each month, although with the decline in interest rates, he has received less. For all but two months out of the entire Financial Diaries study year, he reinvested the interest income he received from this 32-day notice. The two withdrawals that he did take were mostly used to pay for his daughter's university fees.

It also took us a long time to understand that Kenneth Ndola[*] had a unit trust account. He is a well-respected 81-year-old man living in a block of flats in Langa with his 30-year-old daughter, 20-year-old son, and two-year-old granddaughter. He has a job as a caretaker in a block of flats in a different suburb, where he is paid R1 000 a month. This supplements a pension from his previous job of R1 000 a month. His daughter also has a job earning about R1 000 a month. Kenneth's assets are dominated by his home and livestock in the Eastern Cape. He is one of two respondents in the study who have unit trust holdings – we were surprised to hear about this, but he showed us the statements and, sure enough, he had taken a large *stokvel* payment and invested R17 000 in an income fund with one of the well-known South African investment houses. During the study year, he withdrew from the unit trust only once – R5 000 to repair his rural home after a storm.

Pillar 4 retirement savings

Like Mzwamadoda, many households would invest in livestock, but how many of them were either selling or slaughtering the livestock to support themselves in old age? In the urban areas, there was no disposal of assets during the study year, but urban assets, like housing, do not tend to be as liquid as rural ones, like livestock. In Lugangeni, of the 24 elderly households, eight of them disposed of assets (entirely livestock) during the year. In five of the eight instances, they were used for some sort of feast – an initiation or a funeral, for example. In one instance it was used for the funeral of the elderly woman who herself had died. In another, a sheep was sold for R500 – the money was put in the bank and then later used at Christmas and for painting the house. In the remaining two cases, the livestock was slaughtered for the family's use, but it was a relatively small amount of livestock – one pig and three chickens, respectively, and it wasn't every month. In general, therefore, we observed very little disposing of assets to support households in retirement, but we did find that these assets prevented households from needing to dip into savings or borrow to support traditional feasts or one-off expenses.

Another activity which might fall under the Pillar 4 heading is farming, particularly for rural households. However, it is important to note that for none of the rural Lugangeni households, retired or otherwise, was agricultural production an important source of income. Most households did have a garden, but this was primarily for the household's use, not to sell the produce. One exception was a household that sold R900 of farm produce in January and R600 in November. For a household reliant on grant income, which this one was, this was a substantial amount of money, but again, this was the exception rather than the rule. Most households do grow vegetables, mostly maize, some potatoes, green vegetables, squash, dried beans, but it is only enough to supplement the family's own food and not to sell for cash.

[*] Names of respondents have been changed to protect their identity.

Another potential Pillar 4 support might be a small business that a retired person might set up to support his old age. There were instances where a household with a retiree ran a business, but when we looked more carefully, the business belonged to one of the children and didn't contribute much to income. In one exception, an older woman ran a ploughing business using a tractor inherited from her deceased husband, but this year the household didn't use it at all because it wasn't working. In another exception, one of the retirees sold things from her house, but this earned her less than 1% of her monthly income, compared to her grant which paid 92% of her average monthly income.

A last potential way that Pillar 4 may play a part in retirement support is through support from children or other relatives. Remittances coming from outside the households can contribute between 10% and 17% of monthly income for grant recipients (see Table 3), which is a very important form of support. We have less evidence of complete support from within the households. Out of the entire sample of 152 households, and about 650 people, there are only two that could be considered "aged and dependent", with no form of income of their own. This is because most retired people have an old age grant, and often they, with this grant, are indeed the main breadwinners.

In summary, the primary support for retirement tends to come from highly structured instruments, such as the monthly payments from the government old age grant or monthly pension payments. One-off payments from asset sales, retirement annuities or other forms of savings tend to be used for special occasions, to repair homes or for the education of children.

4. RETIREMENT PREPAREDNESS

Households with retirees made up less than one third of the sample, but for the remaining households, and for those working-aged adults who live with retirees, how are *they* preparing for retirement? Not including state-sponsored retirement, like the old age grant, or employer-sponsored retirement, like pension plans, how much are adults saving for retirement?

This question is answered through analysis of the detailed cash flow data from the Financial Diaries. All adult individuals who were working and younger than retirement age were separated into two samples: single adults and married couples.[10]

In the Financial Diaries, cash flows were tracked in and out of financial instruments for all of these individuals, so flows into savings instruments like retirement annuities and pension funds, bank accounts and *stokvels* were used to estimate the amount of monthly savings households were putting aside every month.[11] This monthly savings flow amount was combined with the existing level of assets in the household[12] to calculate a future value figure. This provided, for every adult individual and every married couple, an estimate of assets at the time of retirement, assuming savings flows remained constant.[13] Then, using the current expenditure per capita level observed in the household, inflated until the time of retirement,[14] we estimated the number of years that future value of assets would support the same living standards (expenditure per capita) that each individual or married couple enjoyed at the time of the sample. This gives the number of years of retirement support.

How are people saving?

The results suggest that a substantial part of income each month is going into savings instruments, between 16% and 47%, particularly in Luganeni. What means are households using to save? *Stokvels* and bank accounts[15] tend to attract the largest proportion of savings flows, at least from those who manage to save out of their monthly cash flow (see Table 5).

[10] The retirement preparedness analysis was performed on every individual below retirement age, but older than 18. Anyone going to school was excluded, as well as anyone else who was a dependent and did not earn an income. Also excluded were any households for which we did not have reliable income or expenditure data.

[11] Note that liabilities are excluded from this analysis. This is because we assume that whatever flows are currently going to pay off liabilities will continue to do so. The savings flows that households have managed to achieve during the diaries year, which have happened alongside debt payments, are assumed to continue until retirement.

[12] Income and financial flow data was captured at the individual level but physical assets and expenditure data was captured at the household level. We use the level of financial assets as of the end of the study (November 2004). For families who have adult children who are earning money, we assume that the physical assets belonged to the head of the household and not to them.

[13] Assuming appreciation of the value of the pool of accumulated savings of 5% per year. For married couples, the sum of flows for both individuals was used.

[14] Assuming inflation of 5% per year. We assume that each person would retire at the age of 65. For married couples (who might be the same age), we use the average number of years until retirement. We do not continue to allow for inflation and asset growth after retirement.

[15] Note that the bank account flow data is probably the poorest in the Financial Diaries dataset. Although this data has been checked several times, it was not easy to confirm inflows and outflows in household bank accounts.

Table 5: Percentage of savings flows in different financial instruments.

	Number of households	Monthly savings flows % of income[1]	Percent of savings flows[2] coming through different instruments:				
			Bank accounts	Provident funds	Retirement annuities	Stokvels	Saving in the house
Langa							
Single adults	33	25%	42%	14%	1%	42%	0%
Married couples	13	23%	49%	9%	0%	38%	4%
Lugangeni							
Single adults	25	42%	36%	4%	5%	41%	13%
Married couples	12	47%	35%	15%	4%	37%	9%
Diepsloot							
Single adults	17	16%	44%	12%	0%	43%	1%
Married couples	27	18%	59%	12%	1%	21%	8%

[1]Of those who saved at all.
[2] Savings flows in banks and savings in the house are net, i.e. deposits less withdrawals. All other flows are simply flows into the instrument. There are implications of this for *stokvels*, which are discussed further below.

Will it be enough?

The question is, will these savings be sufficient for people to maintain living standards in their retirement? Based on this analysis, the conclusion is quite rosy. If these savings flows are maintained and all current assets are held and liquidated at the time of retirement, then about 70% of both single adults and married couples will have more than five years of retirement support at the time of retirement. In Lugangeni, over half of single adults and 90% of married couples will have enough savings to last more than 10 years. In urban areas, the picture isn't quite as bright. There are a number of possible reasons for this, including a higher cost of living in the urban areas (particularly transport) and a pattern of sending a portion of earnings as remittances to those in the rural areas. Even so, there are relatively few who would not be able to sustain their living standards for less than one year.

Table 6: Number of years of retirement support

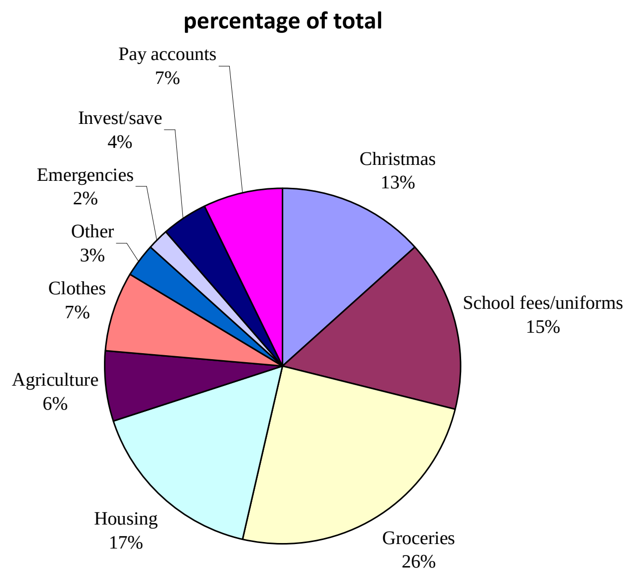
	Langa	Lugangeni	Diepsloot
Single adults			
Less than 1 year	15%	8%	6%
1-5 years	9%	20%	41%
5-10 years	18%	12%	24%
More than 10 years	58%	60%	29%
Married couples			
Less than 1 year	0%	0%	7%
1-5 years	23%	9%	33%
5-10 years	31%	0%	30%
More than 10 years	46%	91%	30%

There are, however, three important reasons why this cheerful picture may be unrealistic. The first is that by including physical assets, this analysis implicitly assumes that these assets will be liquidated to support retirement. This is rarely the case, particularly for housing stock, which makes up the bulk of physical assets. The discussion in Section 3 suggests that even livestock liquidation does not always go towards retirement support.

Secondly, *stokvel* savings are clearly a huge part of savings growth, but most *stokvel* savings are set up to be short term, with payouts being saved and used within a year. The best way to assess what people do with their *stokvels* is to actually observe it, but many *stokvels* pay out in December and we weren't still in the field in December, so we didn't capture this. We did, however, record the intent of what people planned to do. Only 4% planned to re-invest their payout; most had clear spending plans. Note that groceries may relate to year-end festivities, particularly as many *stokvels* pay out in kind, i.e. with groceries.

Of the rotating *stokvels*, most were spent on bigger items, like for a feast, a deposit on furniture, or, often, for parts of a house that was slowly getting built.

Chart 2: Intended use of *stokvel* payment



Lastly, households rarely used built-up savings in the bank, let alone savings in the house, to support their retirement. Therefore, it is perhaps over-optimistic to assume that these adults who are saving now will also keep these savings until retirement.

If we address these concerns by taking out of the calculation *stokvels,* bank account accumulations, saving in the house and physical assets, then how prepared are households for retirement? The picture is considerably less positive (see Table 7), with only about 15% of single adults and 18% of married couples forecast to have greater than five years of retirement support. This suggests that dependence on the social old age grant is expected to continue for some time.

Table 7: Number of years of retirement support, excluding stokvels, bank accounts, saving in house and physical assets

	Langa	Lugangeni	Diepsloot
Adult singles			
Less than 1 year	70%	64%	76%
1-5 years	18%	20%	6%
5-10 years	9%	8%	6%
More than 10 years	3%	8%	12%
Married couples			
Less than 1 year	54%	36%	63%
1-5 years	15%	27%	33%
5-10 years	23%	18%	4%
More than 10 years	8%	18%	0%

5. TWO POLICY IDEAS

Diverting stokvel savings

One has to wonder whether a policy change could help channel more funds into longer-term savings. In the US, experiments with tax refunds[16] have shown that capturing even a portion of this one-time savings flow can effectively help household retain some of the savings they've built up.

Let's say that there was a mechanism that could help capture even 50% of all *stokvel* savings, to be saved to retirement.[17] What difference would that make? The results are in Table 8. Being able to put aside half of their *stokvel* flows would make quite a difference to the proportion of people able to support five or more years of retirement. About 26% of adult singles and 24% of married couples would have more than five years of retirement support if this intervention were successful, compared to 15% and 18%, respectively, if it were not. Moreover, the number of single adults, who tend to save more in *stokvels*, with less than one year of retirement support drops from 70% to 47%, and the number of married couples with less than one year of retirement support drops from 55% to 38%, a drop of one-third in both cases.

Table 8: Number of years of retirement support, excluding assets, bank accounts and savings in the house, but including 50% of *stokvel* flows

	Langa	Lugangeni	Diepsloot
Adult singles			
Less than 1 year	36%	56%	59%
1-5 years	33%	20%	18%
5-10 years	18%	12%	6%
More than 10 years	12%	12%	18%
Married couples			
Less than 1 year	31%	18%	52%
1-5 years	31%	27%	44%
5-10 years	15%	27%	4%
More than 10 years	23%	27%	0%

Financial education

Financial education has become a buzzword among policymakers and supporters of financial access, but nowhere else in the Financial Diaries is the need for financial understanding so clear as it is in the case of retirement and life insurance policies.

[16] See Tufano, P. (1997) "*Just Keep My Money! Part I The Potential for A Refund-Driven Savings Bond Program* Working Paper, found on http://www.d2dfund.org/news/research.php, and Duflo, E, Gale, W, Liebman, J, Orszag, P, and Saez, E. (2005) *Savings Incentives for Low- and Middle-Income Families: Evidence from a Field Experiment with H&R Block* NBER Working Paper No. 11680.

[17] Not that this is by any means an easy policy to carry out. Stokvels pay out at very irregular times and are themselves very amorphous institutions, changing all the time.

Of the many households that had retirement annuities, provident funds and/or life policies, only a few knew what these instruments were for, how much they could expect and when they could expect it to be paid out. Mr. Ndoli[*] is an excellent example. He is 59 years old, living with his two children and sister-in-law in a hostel in Langa. He's worked for the same engineering company since 1969. He now earns a gross salary of just over R1 000 a week. Every week, he contributes R73 towards a provident fund. He first started contributing to this provident fund in 1978. He had no idea why this money was being taken off his payslip or what it meant. He didn't want to ask his employer for fear of losing his job. We decided to try to estimate what had accumulated in his provident fund and how much he might have when he retires. We assumed that his pension contribution most likely increased in line with his salary, which probably increased in line with inflation. Based on that assumption, even with no capital appreciation, we estimate that he should have about R75 000. With even a modest 3% capital appreciation, not allowing for inflation, he would have R110 000. When we told this to him, and showed him our calculations, he was so surprised he sat down and couldn't speak for the remainder of the interview! He later told us that he hoped to buy a taxi with this money when he retired to the rural areas, and this would support him and his family in his old age.

We found Mr Ndoli's story entirely typical of our sample. No one knew what the deductions for the provident fund were for, how it worked and what amount they might expect. When asked why they did not ask their employer for details, the response was they did not want to lose their jobs.

In the same way, we also found households that had numerous life policies and retirement annuities, and many did not know what each was for. Worse, they had no documentation that would help us explain it to them. Many teachers and nurses signed up for policies when company representatives came to see them at their workplace. However, very few of these people understood what they were signed up for, which resulted in some households being far out of balance in their portfolios, with too much life but little retirement savings.

One of the first steps in making retirement planning work for low- and middle-income households is to start financial education in the workplace, so employees know what policies they have and how they will benefit from them. The Financial Services Board could play a bigger role in making sure the sales of retirement instruments included full disclosure. Most importantly, for employer-run provident and pension schemes, staff need these plans explained more clearly and regular updates to tell them how much they have accumulated. The Department of Trade and Industry could do more to ensure that this happens effectively. Ultimately, the trustees of all retirement funds have the fiduciary responsibility to communicate clearly with the members of the fund and to make available appropriate resources to address any questions that members might have in an open, non-threatening environment.

[*] Names of respondents have been changed to protect their identity.

6. GUIDANCE FOR FUTURE RESEARCH

FinMark Trust wishes to understand the extent, availability and appropriateness of South Africa's retirement savings vehicles. The richness of the Financial Diaries dataset goes some way in allowing us to understand the household, or demand, perspective on retirement savings, not only in considering pensions and old age grants, but also private savings for retirement including some sources of Pillar 4 funding. However, the limitation of the Financial Diaries is its small sample size. With only 152 households, drawn from three areas, it is impossible to determine if these results can be generalised across different populations.

Focus groups may be one way to extend our understanding of whether the results found in this report are representative of other low-income groups in other areas and among other race groups. This report may be useful in developing a pilot questionnaire for such an exercise.