Pre-retirees can mitigate reduced retirement benefits brought on by Covid-19

By Chan Choong Tho and Chan Fook Leong

THE 2020 CFA Institute Mercer study, which examined 39 retirement income systems and covered almost two-thirds of the world's population, had a grim conclusion: Retirement benefits will likely be reduced in our advanced years due to Covid-19. The respiratory pandemic ushered in a global recession which slammed employment and reduced contributions to public and private pension systems. Three other factors exacerbated this grim situation – a fall in investment returns, lower future government support, and an increase in earlier access to retirement benefits.

What now for pre-retirees?

Working longer means the current expenses and obligations continue to be met with current income, and drawing down from reserves is unlikely. For most people, the additional income from continuing to work is likely greater than the extra returns from taking on more risk in a portfolio. PHOTO: AFP

Save more

Many of us do re-examine what is deemed a want compared to a need in times of an economic crisis. For example, we may consider selling off the family car which many deem a luxury. Nevertheless, others differ and deem the car as a necessity. We know it makes it more difficult that having had access to a car for several decades, not having one now may elicit jibes from relatives especially during family gatherings. Within the extended family, owning a car may have the effect of elevating one to a certain social class.

But getting rid of the car saves petrol, parking, ERP charges, maintenance and monthly loan repayment. That is not insignificant and could potentially boost savings per month, although that sum would be partially offset by the cost of public transport.

Take more risk?

Even pre-pandemic, many lament the low deposit rates. With the global recession brought on by the pandemic, central banks and governments have taken on even more debt to cushion the pandemic's devastating effects. Central bankers are expected to maintain accommodative monetary stance for years. Hence, do not be surprised if banks in Singapore continue to maintain the all-time low rates for an extended period of time.

A pre-retiree may mull over taking on more risk to bolster returns, such as investing in equities, unsecured junk bonds and structured products.

There are a couple of major considerations before shifting substantially more funds into riskier assets:

- The ability to take on more risks declines with age. Should there be losses, pre-retirees do not have a long runway to re-accumulate wealth through employment or entrepreneurship
- Understanding more complex risk assets. We may not be at a level where we can reasonably understand how the assets work, generate returns and the risks associated with those instruments
- Financial position and family members who are deemed dependents. The weaker the balance sheet and the more the dependents, the less able are we to assume more risk

Work longer – the uncomfortable truth

We left this important section to the latter half of the article as it may be contentious and can stir up strong emotions. We view working longer as a viable alternative to accumulating adequate funds for retirement. But we also understand the strong reaction this suggestion may evoke. Many may want to leave the stress associated with a career.

Perhaps shifting to a less stressful position will be more palatable for most who contemplate working a little longer.

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Gainful employment also means that one continues to accumulate retirement funds. A pre-retiree can continue to build on his or her CPF retirement account. And hopefully, there are intangible benefits such as fulfilment and healthy social interaction which humans need and thrive on.

Jacques Lussier, CFA, wrote in a 2019 monograph by CFA Institute Research Foundation titled "Secured Retirement": "The absence of uncertainty makes retirement planning easy. The solution is straightforward if you know when a participant will start saving, what portion of his income he will save, how his income will grow, what level of real returns financial markets will deliver on average, what the patterns of returns will be, when participants retire, how healthy he will be, and how long he and his dependents will live."

The world we live in is uncertain. This was highlighted rather cruelly when Covid-19 turned our lives topsy turvy. It makes retirement planning hard. In the ongoing pandemic, we do not suggest pre-retirees settle for poverty; nor do we suggest taking more risks than one can stomach. We do suggest separating a need from a want. Saving a little more over the longer term makes sense for many. We also suggest working longer and having a fulfilling second career or job as the way forward.

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