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Disrupting strategies to fulfil **retirement goals**

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Will the value of your retirement income ensure that you live the comfortable life you have become accustomed to at the later part of your work life?

It's not about the value of your accumulated savings pot and investment returns, but about retirement goals and the value of your future income.

This is where South Africa-based liability-driven investment manager Colourfield and Nobel prize-winning economist, University Professor Emeritus at Harvard University, Robert Merton, say the future of retirement plans lies.

Merton, a resident scientist at Dimensional Holdings, was this week hosted by Colourfield in SA. Speaking to *Finweek* at Melrose Arch, Johannesburg, he emphasised the importance of Defined Contribution (DC) retirement plan strategies shifting from focusing on accumulated savings and investment returns, to an individual's investment goals and implementing strategies to ensure their money grows to reach their targeted value of future income.

Colourfield, in partnership with multinational investment firm Dimensional Fund Advisors LP (Dimensional), is finalising the launch of a localised DC retirement plan solution to meet SA's retirement and pension funding challenges. The plan is expected to be launched in the next six months, according to Colourfield.

Colourfield CEO Costa Economou says the industry at large is mostly not aware of this goal-based retirement strategy. That, he says, is why people are retiring with inadequate levels of savings.

Economou says a person aged 40 or 50 with a retirement fund will most likely be confident they have enough savings. But calculating their future income when drawing closer to their retirement only makes them realise that what they thought was a substantial asset (maybe worth R1m or R1.5m), when converted by an insurance provider or annuity provider into pension, is substantially less than their current levels of earnings. In order to put things into perspective

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Merton says eight to nine years ago in the US, a person that did not want to take a risk would be referred to taking a Treasury Bill (an equivalent to a SA government bond), which would be guaranteed by the government. At that time it would have gotten you growth of 4% to 5%, so on $100 000 that would be $4000 to $5 000 per year. Even though today the amount invested is still $100 000, you will get one tenth of 1% on that Treasury Bill, which is only a $100. Why? It's not because the value of your money lessened due to inflation, but because the interest rates came down, says Merton.

"The investor focused on the $100 000 and the money is still worth $100 000. The safety has been fulfilled,

Robert Merton
University Professor Emeritus at Harvard University.

but the problem is as a member you care more about the income you could live on [in retirement]. The investor did the right thing with the wrong measure," says Merton.

He says this could be misleading to people since the wrong measure of risk is used. "There is a need to change for DC, we have to recognise that the goal is [retirement] income. We have to measure risk in terms of that income, not in terms of the value of the portfolio," says Merton.

Merton says that the risk should not be based on the fund member's age, but on how close the individual is to reaching their retirement goal. And once the retirement goal has been reached, the risk can be lowered.

Economou says most boards of trustees they have spoken to are hungry for this sort of strategy and they are confident it will resonate well with what they want to achieve for members of retirement funds. ■

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