

# Forum on CPF and Retirement Adequacy

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# Balancing Returns, Risks, Facts and Fallacies: Observations on a Worry-Free and Sustainable CPF System

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“Balancing Returns, Risks, Facts and Fallacies: Observations on a  
Worry-free and Sustainable CPF System ”

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## The Low-Down Facts on Stocks

- Diversification helps but that does not mean a well-diversified basket of stocks are as safe in the long run. If they were safe in the long-run:
  - they wouldn't command an "equity risk premium"
  - Warren Buffet would be offering downside insurance on stocks which "premiums" becomes cheaper as your investment horizon increases!
- To paraphrase Nobel laureate Robert C. Merton, a goal-oriented approach to retirement planning is warranted...
- ...and getting one's objective function right is paramount

# World Cup Fever: Goal-based Investing

## Asset/Liability Management 101

- Determining the appropriate **objective function** (or the “goal”) for any portfolio is important:
  - Example 1: Goal is to provide for four years of tuition fees and lodging at a university, beginning when your child is 18 years old
  - Example 2: Liability-driven investing (i.e., buy bonds!) with the goal of repaying targeted liabilities (or payouts) according to a schedule, as in a **defined-benefit pension fund**
  - Example 3: A managed **defined-contribution** product where the goal is to receive inflation-protected retirement income for life, adequate to sustain a dignified standard of living from the point of retirement

## It's getting harder all the time: The retirement problem

- The average investor is concerned about 3 fundamental issues during retirement:
  - Receiving a reasonable, level payout every month
  - It should last for as long as the retiree lives
  - It should be indexed to his or her cost of living

## Myths, Urban Legends and Facts about the CPF

- Myth: There's nothing wrong with socking away 36% of your salary in risk-free assets for retirement purposes. In fact, we should be celebrating the fact that Singapore and Malaysia have such mandated social security savings schemes for the longest time ever
- Fact: Start saving as much as you can for your retirement as soon as you enter the work force
- Admonition: DO NOT encourage our citizens to dig into their retirement pot (which is meant for expenses and health care needs in retirement) to finance our kids' education and that dream HDB home along the way. These should be run as separate tax-advantaged programs, like in the U.S.
- Take Away (or "TaPao"): CPF Life is a good **life annuity** program for all. It should remain the default, worry-free funding program that guarantees Singaporeans a dignified standard of living in retirement. But it should be **inflation-indexed** – is this the next change?

## Inflation is Inflated...

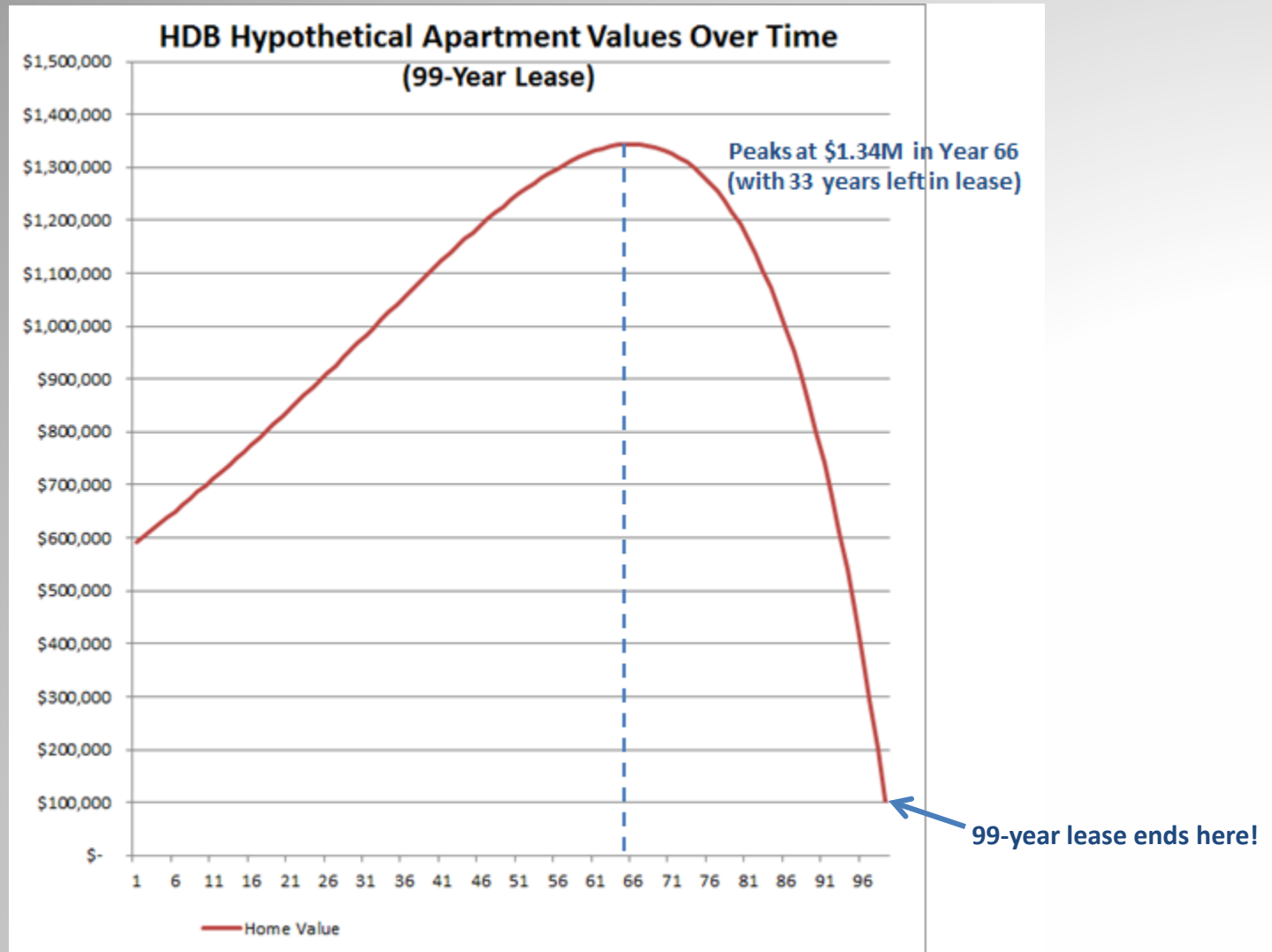
- Myth vs Reality Check: True inflation in Singapore – a.k.a. MAS Core Inflation, which excludes the cost of private accommodation and transport – is around 2.0 percent per annum on average
- The first \$60,000 of your CPF combined balances in the SMRA can earn up to 5%. The 30-year SGS bond is currently yielding ~3%
- So you're already beating inflation by about 1% if you invest in the 30YR SGS bond, and by about 3% (on a pre-tax basis, post-tax it's even higher) on the first \$60,000 of your CPF combined balances
- Please call me if you know of any other (good) government that's currently effectively offering a (tax-free) 3% riskless real yield



## Say RA-RA-RA (Retirement Adequacy)

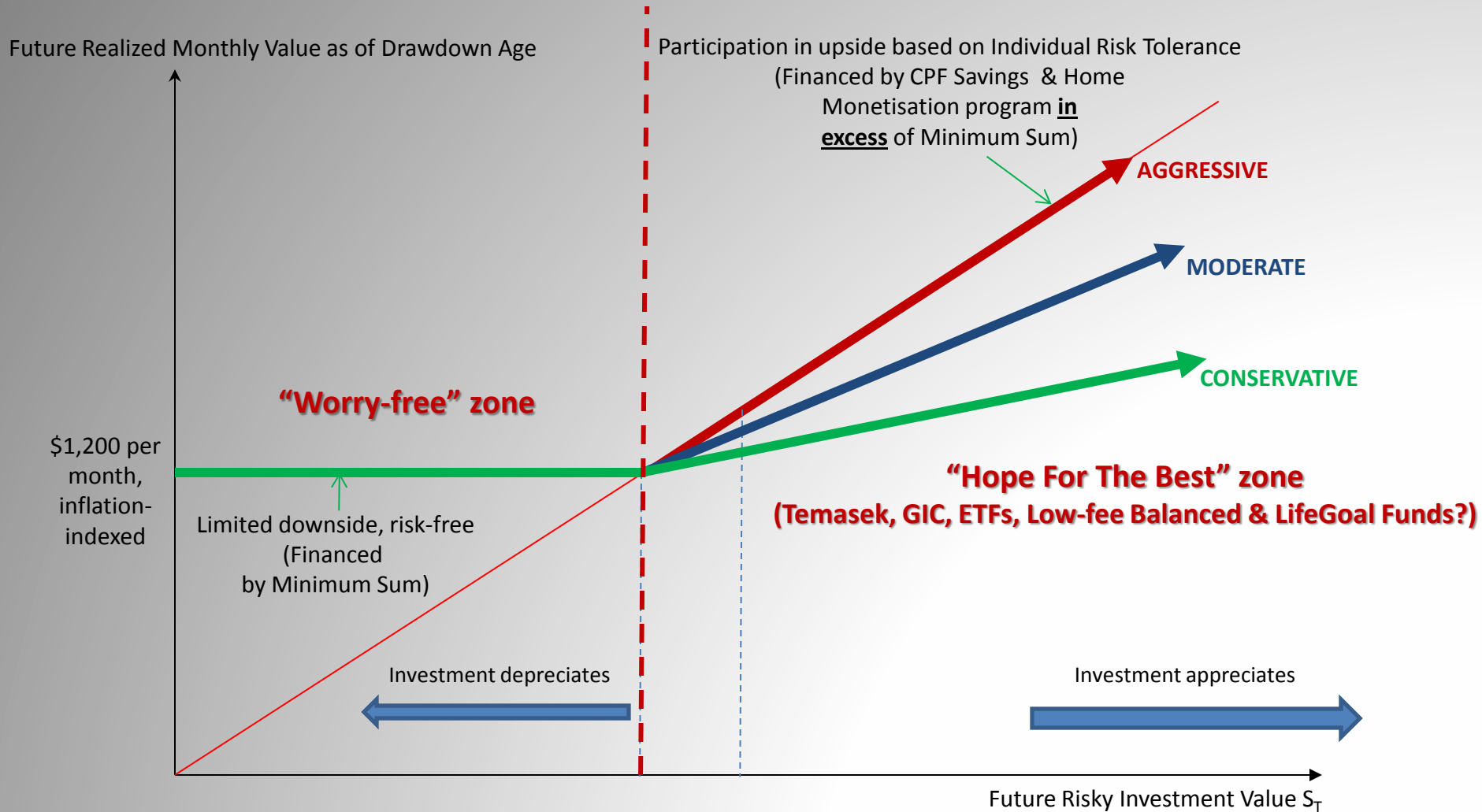
- Home monetisation schemes to supplement one's retirement income should also be for Life. Example, the HDB 30-year Lease-Buyback Monetisation Scheme should guarantee participants housing for Life
  - Would anyone here want to enter a monetisation program at age 62 where, God-forbid, you live to the age of 92 to find out your HDB Lease-Buyback scheme has expired and you may have to move out? (Moral: Avoid shòu 寿 risk)
- Singapore also has the privately-managed Supplementary Retirement Scheme (SRS), where Citizens & SPRs can contribute up to S\$12,750 per annum with full tax breaks
- Allow spouses, example, fulltime housewives or househusbands, to participate in the CPF on equal terms as the working population. Give families who'd like to save more for their retirement, the ability to do so
- Synchronize the CPF "Withdrawal" / Minimum Sum Age (55) and the CPF Life Drawdown Age (60 – 65) to the later date so that retirement savers have up to 10 additional years to catch-up on their savings and meet the Minimum Sum (at their **Drawdown Age** and not Withdrawal Age)

## Oh, Give Me a Home on The Range... (The Reality)



Source: CAMRI (Simulations based on assumptions made w.r.t. rental income , growth rates, discount rates, etc.)

# CPF (SoShiok) Life Product: Inflation-indexed with Upside Potential



## Some Parting Thoughts

- Keep messages to the citizenry about their retirement savings, health care, and home monetisation programs simple to understand and transparent
  - Trust increases with transparency, open communication and frank dialogue
  - Trusted elders of our society could be engaged to conduct some of the communication programs on retirement and the need for the CPF
- Integrate health care and other forms of life & death insurance into the retirement savings equation. That also appears to be the “next change”
- The CPF Minimum Sum of S\$155,000 yielding S\$1,200 per month for life (risk-free) via CPF Life is actually a very good payout, based on the maths and current discount rates. The question: Is S\$1,200 enough?
- However, please do consider offering a **CPF SoShiok Life** product, which is inflation-indexed on the floor (=dignified standard of living payout) and allows for various levels of participation in upside returns (if any)