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Please note that for the cameos in this book the names and some situations have been changed to avoid identification.

Section 2: The yesterday person

At retirement

In this section we are going to explore:

- Emotional states and coping mechanisms
- The right time to retire
- Lifestyle changes
- Choosing an annuity
- How to use annuities.
- The cost of advice and management fees.
- Creating a new paradigm- consulting, new businesses, hobbies, travel, fixing the house/downsizing

Chapter 1: Retirement

The dreaded or anticipated day has arrived. This is where the pedal hits the metal of the retirement car you have chosen to drive. Decisions have to be made that have to be the right ones. Except for the very rich, most retirees will have no room to manoeuvre, after they make the choices in this step.

Emotions
A whopping seventy–one percent (71%) of pre-retirees want to continue working. In case you're wondering-this number includes those who have prepared for retirement. Companies that are prepared to continue the employment with flexible work hours are valued for the stimulation and satisfaction. Often the retiree will state this is of a higher value than the actual pay check after retirement.

The truth is that retirement can be terrifying, even for those who have a good retirement income. For those who have a reduced income, it can be overwhelming. Money is naturally the one major consideration, but the ability to interact with human beings on a professional level fulfils a need in all of us. This social interaction is of prime importance.

At Retirement, there is an emotional rollercoaster ride as the sudden realisation hits, that there is no regular income with annual increases and 13th cheques. The first worry in the immediate future is how to pay monthly household bills. This realisation is coupled with the loss of those people you interacted with every day of your life. The initial period before the actual retirement may not be sufficient to come to terms with the enormous life style change. A process of grieving will begin. Denial and shock may be in the start of the process, rapidly followed by anger and frustration. The anger and frustration may display as pain and guilt, the health, possibly, will suffer. Such emotions require a pattern to be put in place to ensure regular, healthy sleep. A lack of sleep diminishes activity in the frontal lobe, which is associated with impulse control.

How can a person ensure they get sleep? Put in a routine to calm the brain down around a half hour before bedtime. Breathing exercises can help to calm the person down. Milky drinks, honey or herbal calming baths and drinks can all help. In ethno-medicine we use lime blossom in the bath and we may even give the person a banana and honey tea. Psoralea pinnata, camomile, lavender, lemonbalm and passionflower are all calming herbs which may be used. A visit to a herbalist or your doctor may be needed if sleep is elusive.

Be aware of the dangers that you could fall into, as this period unrolls. Addiction is common in this phase, the person may become addicted to things such as sport, ill health, drugs or alcohol.

This period however should pass quickly, if you are aware and alert to it and in the maturing process our next step will see the person bargaining with life, by reforming the lifestyle, selling the house, buying a 4x4, travelling or even helping out at a charity. However depression often follows as the feeling of self-worth erodes with the grey hair. Depression is also felt due to the death of family and friends. We will look at this stage in our section on post retirement. Just understand you are not alone. Many people battle to get to an acceptance stage, where they burst out the chrysalis of work life into the butterfly stage of retirement with purpose. The acceptance stage can be seen when the person embraces a retrospective view and stable emotions. They look forward to the future with a sense of responsibility and purpose.

Emotions as you see, will play a huge role in how you plan for your retirement at retirement.

Bob and Ellie both worked until his retirement. They were financially well –off and considered retirement to be a chance to explore their beautiful country. At first they went away, but then Bob got consultancy work and did not know when he was needed, so he ended up wanting to be at home, in case work came in.

Ellie became increasingly frustrated being stuck with Bob as her sole companion. Bob had become a couch potato, more than an intrepid explorer and consultant. Ellie now began to be increasingly angry with her life. This anger worsened when her eldest child moved back into their house from overseas with her two children and a difficult husband. Ellie felt used and abused. Her health began to suffer and soon she had full blown diabetes.

Ellie now had a reason to say she could not do the things she was expected to do. Her blood sugar swings pushed her into frequent comas. Despite the hate she professed for the disease, she enjoyed the attention and the caring she was now getting. The daughter decided to move out the house far from her mother- this was a blow, as Ellie enjoyed the children's company, so long as she was not expected to clean up and feed them. Eventually the son-in –law moved the family out of the country as he was offered work offshore. Ellie again had to clean up the mess they left behind. She became angrier and the anger created more health problems. Bob became her full time nurse and had his hands full with her mood swings, forgetfulness and sugar management.

It became a real problem for Bob. He was not the type of person who was suitable to be a nurse, although he had stepped up to the plate, he also disliked his life. Things came to a head when Bob had a stroke and suddenly Ellie was having to cope with the loneliness and a husband who could no longer walk properly or drive her around.

Ellie was fortunate in that she had access to exceptional psychological advice, from a person who knew the family well. On this person's advice, Ellie met with her brother, who then asked the two if they could help him in his business. This was to give the couple a purpose in their life. Her brother responded with gratitude as the finances were in a mess. Ellie was a very proficient book keeper. Although her brother could not afford to pay her, it gave her the reason to start driving in order to manage the office. Bob came with and pretty soon was found fixing up the business property. Today Bob and Ellie still work at the brother's business in managing it, but have their own lives back. The two of them have started organic gardening in their own property and are enjoying their lives far more than 5 years previously. Ellie still has brittle diabetes, but modern technology helps her to monitor the disease. She has also joined a Pilate's class and both her and Bob have a sympathetic chiropractor. The Chiropractor was a person whom they knew well as a child, which allows them to talk to her, not only to help with the aches and pains. The chiropractor ensures she has long appointments for the two as she recognises their need for both social and physical interaction.

Ellie's take away is that you need the right people in your life, as money is not sufficient to give a person purpose. She knows now, that for her and Bob, family is important, but there also has to be a line in the sand. They have the line drawn- it allows them to help the family, but not to be taken advantage off.

Finances
Why do we have to plan in retirement for retirement at retirement?

At retirement you change the retirement or pension fund lump sums into an income producing stream, called an annuity. Scary facts tell us that 40% of retirees take just 2.4 years to deplete the lump sum benefits they have provided. Source I used is Sanlam's 2016 benchmark. For many people being given the lump sum is overwhelming. The sum appears larger than the income it can provide and temptation to spend it may override common sense. It is also not unusual for family members to just need a little help as you hit retirement, and the promises to pay back the money may not be fulfilled.

Pensioners have to make certain choices before retirement. While you are in the emotional pre-retirement stage you have to decide on annuities prior to retirement. For those lucky enough to have a defined benefit pension funds, giving a defined income, the chance of getting a similar performance outside the pension fund on those monies, is often slim to none. In the defined benefit fund the income is known and is fairly safe. You should try and reduce your spending to match this amount. For a person in a defined benefit fund retirement does not have to be timed. For the rest of the population we have to look at a variety of different methods to insure an income.

Timing of retirement

On retirement there may still be liabilities owing. Liabilities include all financial obligations (housing bonds, debt) as well as family obligations. Liabilities where possible should be paid up before retirement, unless the return on investment exceeds the cost of the liability.

The income choice has to be made between a fixed or conventional annuity and the living annuity. We will look at annuities in detail in our next chapter. Before we choose we need to not only understand the annuity but also inflation expectations. We will also have to understand bond prices and interest rates which in turn affects the cost of a purchased annuity.

If you are in a defined contribution fund, try not to retire when the economy is down and in a bear market. A Bear market is where the share market is losing money. A rising market is preferred for retiring if you do not have that defined benefit fund.

Timing, when you buy a fixed or conventional annuity is critical. If inflation rises, interest rates tend to go up, and the cost of the annuity falls, so you receive a bigger monthly income for your lump sum. You ideally want a high interest rate for the purchase of the annuity. If you have to retire in a low interest rate environment, make use a living annuity, until the market changes and then if required, buy into a fixed or conventional annuity, when annuity rates rise.

An annuity is a financial product sold by insurance or pension companies that pays monthly, quarterly, bi-annual or annual payments to a person, for as long as he or she lives. Annuities are usually purchased by investors who want to secure some type of income stream during retirement. Which annuity you get, will depend on your financial knowledge and the capital you have accumulated. Annuities vary considerably. We will look at these in more detail later in the chapter on annuities.

Annuity rates vary considerably as a result of age as well. A fixed annuity amount will vary between insurers and a million will normally buy around 6000 per month at age 65 for a male or 5 400 for a female. There is up to a 3% per annum increase, in the amount an annuity will pay, for every year you delay retirement. Planning at retirement must take into account your life expectancy. This is crucial to you at the point of retirement. Those in good health may feel they will continue to experience such a situation, while those who are sickly may decide to have a reduced annuity. Both approaches may be wrong.

It is not unusual for a retiree to have the need to reduce the lifestyle substantially due to retirement. Budgeting during the period, before retirement, takes a lower priority to after retirement. This is due to life style changes that take place when we get more income, due to career progression and less expenses, as children and other dependants no longer are a continual drain on the finances. In addition we often forget the impact of the life changing events, which may happen, such as a marriage of a child or frail care for a parent. These payments can dramatically impact on a retiree if not planned correctly.

When the income from the annuity starts to reduce, the pensioner may not find another job due to age discrimination in the work place. Contract work may not be easy to find given the current economic environment except for those with essential skills. What will worsen this scenario are the technological advancements that lead to our longevity, as these also result in one of the top expenses for us all in retirement, namely a medical scheme or medical health care.

When hitting the expenses, an immediate kneejerk reaction is that many retirees decide to cancel their existing risk policy contracts as a quick solution, to increase affordability of higher priorities. This could result in you becoming uninsurable, if you want to buy another property to rent out, or open a business and obtain a loan. In order to understand our situation, let us look at the tools we normally use at retirement.

From pension to income

This period at retirement marks at what we call the "Decumulation Phase". At this point you have to start living from the balance sheet and not from an income statement. Effectively you can deplete your capital very fast. In this book we are going to look at that very carefully in our section on post retirement, to help you not run out of money.

Your pension fund may have an offering of an in fund annuity, which is normally linked to a large fund or an out of fund annuity. Out of fund always means the fund is run via an insurer and this has certain implications for the retiree

Out of fund means the annuity is not subject to any Pension funds Act and so can be left to any person, if a living, death benefit or guaranteed period annuity is bought. The risk to the person taking the annuity is that the insurer goes out of business. In fund, the fund will first apply the requirements of the relevant pension and tax acts, which normally means they need to look at the dependants first and only then does the balance of monies go to any appointed persons, these persons are named the beneficiaries. Another major difference is an in-fund annuity cannot include any external funds you may have saved, while the out of fund can take these savings into account, this may help in negotiating of the costs of the fund management.

The pension fund will normally request a PRI (post retirement interests) from the member in order to give advice as there are a number of annuity options, all dependant on what you actually have saved.

Pension fund annuities mean there is a written agreement, between an insurance company and a customer, outlining each party's obligations in an annuity coverage agreement. This document will include the specific details of the contract, such as the structure of the annuity – does it pay monthly or quarterly or annually. It will also specify the amount payable for that period. The agreement will list any penalties for early withdrawal, (if that is permitted), spousal provisions such as a survivor clause, and rate of spousal coverage, and more. Pension funds will buy an annuity with the lump sum for the member on retirement from the fund. In some cases this is a legal obligation, while in other situations the setup of the fund will determine the obligation to purchase an annuity. Countries also will have different requirements; for example, in the UK income based levels determine the requirement to buy an annuity with 75% of the lump sum from an approved fund.

South Africa currently, does not require a provident fund member to buy an annuity at retirement. The same situation will be found from existing preservation funds and you can take a single withdrawal, if you need cash to supplement immediate lifestyle costs, without withdrawing from the fund before retirement.

All withdrawals from any fund will be subject to a lump sum taxation, with an initial amount allowed tax free and the balance taxed on a table that is set by the tax authorities. Once tax is paid you cannot get it back, so it is advised to ensure that only the tax free amount is taken as a lump sum or the minimum amount you need. This tax free amount is a once of amount allowed throughout the individuals life time, and will be reduced or even non-existent, if you took a withdrawal before retirement, such as on a retrenchment package. Withdrawals from both a provident and pension fund may be taken on leaving a company, retrenchment or retirement depending on the country you are in.

Other retirement funds

Personal pension funds have many names ad flavours. These are individual retirement funds taken outside the employment or compulsory country retirement savings requirement, for additional retirement savings.

Individual retirement funds are known as private pension funds or retirement annuity funds. Retirement annuity is the name to the pre- pension saving and they are so called because the funds have to be used to purchase an annuity after retirement subject to certain conditions. In the USA there are a variety of Retirement Annuity accounts used by employers outside the 401 (k) plan. The USA will also use Keogh or HR 10 plans.

Individual retirement funds differ depending is they are approved or unapproved by the tax authorities as retirement plans in that jurisdiction. Plans that do not meet the guidelines required to receive a favourable tax treatment are considered nonqualified and are exempt from the restrictions placed on qualified plans.

International retirement plans are found in jurisdictions such as Guernsey. Guernsey is a favoured spot for Individual retirement funds in Sterling, Euro, or US Dollars. Income and capital gains arising from the investments held within the plan, or benefits paid by the plan, are not subject to Guernsey Income Tax.

At retirement you may decide to make existing approved Individual retirement funds /Retirement Annuities (RA's) paid-up. Again depending on the country, the condition of the approved Retirement annuity is normally to buy an annuity with majority of the lump sum. This annuity is based on your lump sum and pays you an income. Depending on the type of annuity the income should be paid until you die or run out of money in the capital (lump sum) account.

While the pension or provident fund may be dependent on age and necessity to take a partial or full withdrawal, individual retirement funds or retirement annuities, in most countries do allow for later retirement with higher limits on membership than the employer would have. Allowing for later retirements has a benefit to these funds and the people investing in them, as it allows a longer period of contributions. Before you do convert your individual retirement funds /retirement annuity, please do a financial needs analysis prior to retirement and if necessary choose to receive financial advice in retirement.

We will look at the various annuities you can buy and which are readily available in the next chapter.

In our section on Managing the finances we will look at the various investment types to help you understand how you should invest to make the money last.

Chapter 2: Annuities- the choice is yours

In an annuity the insurer or pension fund will be concerned on the capital amount you bring in and the amount they have to pay out. To calculate this the insurer will use a table which is worked out to give the average life expectancy of each person applying for the annuity. This way they can take a calculated risk that the capital you bring in will last for the annuity in your life time. The risk to the insurer is that you will outlive your expected life span. We call this risk longevity risk- the risk of a longer life than expected.

Annuities may be bought with funds that legally have to be invested and funds that are not required to be invested, such as your private savings. It is normally beneficial to invest in these voluntary annuities as the taxable income you receive is weighted to discount the lump sum amount put into the fund, while capital gains and dividend tax is not levied on the fund, resulting in a higher return per currency unit invested than you can get privately.

There are two main types of annuities:

- Immediate annuities.
- Deferred income annuities.

Immediate annuities

When you make a lump-sum payment to an insurance company upfront, you receive the right to receive payments from the insurer on a regular basis beginning immediately. The payments are based on factors such as life expectancy and interest rates in force at that point.

Deferred income annuities.

For certain people retirement actually means changing the pension fund into an annuity they do not need at that point. Insurers recognise that when a person has to retire from a pension fund, they may need a vehicle to put the money into, but not a vehicle that gives them an income at that point. Deferred annuities are used for this. You pay a lump sum upfront amount, and in exchange, the insurance company promises to pay you a certain amount once you reach the age specified in the annuity contract. These annuities effectively reduce the tax payable as the income from an annuity is taxed at the person's marginal rate to a deferred date when the person will not have such a high income. These annuity type products carry surrender charges, limiting cashing out and ongoing annual fees.

Both annuity types have various options, we call these options flavours.

Fixed annuities**.**
When you put a sum of money into a fixed annuity the value you will receive on payment is based on stated returns within the annuity contract. Typically, fixed annuities don't have payments begin right away and are therefore deferred annuities, but unlike a deferred income annuity, you retain the flexibility to choose if and when to start receiving payments from the insurance company under the contract.

Variable annuities.
When you put a sum of money into a variable annuity. The value you will receive on payment is based on market returns. In other words it varies according to the returns received. Again this annuity operates like a deferred annuity, but you retain the flexibility to choose if and when to start receiving payments from the insurance company under the contract.

Now we have an idea about the annuity product we need to deep dive into the flavours or forms used to create these annuities.

Compulsory annuities
Compulsory annuities are bought with the legally required amounts for the pension fund. You may receive a different income for the same amount invested, so you should shop around for the best available rate at the time. The only time your choice of annuity will be limited is on a defined benefit fund as the fund guarantees the annuity amount on retirement. The annuity the fund will give you is normally about the best you can get- however you do lose the capital amount if you die. This situation is a problem if you have a spouse or if you have a dependant such as a mentally challenged child.

Unless the compulsory annuity has options to provide for a dependant, you should consider moving any non-compulsory annuity amounts into another company, which will provide for both parties, without a tax implication on the withdrawal. We call these product voluntary annuities.

There are a few types of such voluntary annuities.

Life annuity

A life annuity is a financial product sold by insurance companies that allows you to swop a lump sum of money and to trigger a stream of future income payments. Life annuities provide an income stream that you cannot outlive. It is a promise for life. However it does not necessarily pay the same income for life- this will depend on the annuity structure. Insurers have a fairly good estimation of your lifespan by using mortality table.

In a life annuity, the insurer will pool all annuity customers together. Once you die the annuity ceases and nothing more is received from the insurer. The risk in this type of annuity is that you (or, indirectly, your heirs) forfeit your savings, in the event that you die sooner than expected (unless a guarantee or life assurance is built into the contract). Annuity rates can differ from company to company as well as from month to month. A quote for such an annuity is only honoured when the cash is deposited with the company. This process can take up to six months after you have informed the pension fund that you wish to move your funds to another company. Most quotes are valid for a certain amount of days.

Be doubly careful that you insist that should the annuity rate go down, you wish to have the right of refusal, because once the money is in the fund – you cannot move it. Insurers in my bitter experience, tend to place the money on it arriving in their account but do not check the annuity rate is the same or better than you were given. Fluctuations can be wide. In my case I found fluctuations of 2% on a return on one hundred thousand (100 000) currency units. In other words that is 2 000 per annum you have lost for the rest of your life.

Guaranteed life annuity

A guaranteed life annuity are those annuities that are bought without an expiry date – the annuity you purchase must provide you with an income for life. The annuity you receive therefore factors in your life expectancy at the age you take out the annuity. The younger you are the lower the annuity you will receive. The annuity is in effect an insurance policy that protects you from the risk of longevity and low market returns. The drawback is that your capital dies with you, and no money passes onto your heirs even if you die the next day after signing the annuity agreement.

Guaranteed and then for life annuity

This annuity will pay out less than the guaranteed life annuity product, as it shields you from the risk that you die soon after retiring and thus forfeit the bulk of your retirement savings to the life assurance company. This annuity (fixed or variable) is guaranteed for a set number of years (typically between 10 and 20); should you die within the guarantee period, your heirs will continue to receive your pension for the remainder of the guarantee period. You will continue to receive your pension after the guarantee period, but the payments will then stop upon your death (i.e. your heirs no longer benefit).

Level or fixed annuity

In a fixed or level annuity, you receive the same amount every month for the rest of your life. This means that your income does not grow with inflation; the purchasing power of your annuity (and hence your standard of living) will gradually decline because of inflation.

The choice of a level fixed annuity should only be used if you are banking on not surviving much past a 10-year period and you do not have dependants. This annuity normally gives the highest upfront payments.

Escalating or variable annuity

This is a most expensive annuity initially as it will pay less than the level annuity. This annuity increases annually, either by a fixed amount, or in line with a pre-determined inflation index, such as the Consumer Price Index (CPI). An escalating annuity will pay out less than a level annuity initially, but will maintain its purchasing power and thus gradually overtake the fixed annuity in value. Within 10 years the level annuity and inflation-linked annuity usually break even and the inflation linked annuity will start to outperform the level or fixed annuity after this period.

Annuity's with profit

Often considered the next best option to an inflation linked annuity as above. The profit linked annuity normally cannot give a pension increase of less than 0%, but will depend on the market performance. If the market in which the insurer is invested performs badly, then the profits may not allow increases for some years. Pension increases are subject to smoothing, where the life assurance company holds back some of the profit made in high-return years, to soften the blow of low-return years. There are higher costs related to this annuity and there will be conditions attached to it. This is an escalating pension, guaranteed for life; however, the rate of increase is not guaranteed and depends on the net (after cost) investment performance of your initial investment. Increases are declared as bonuses; and once declared, become permanent (i.e. part of your guaranteed pension).

Capital-back guaranteed annuity

This product combines an annuity (fixed or variable) with a life policy. The annuitant uses part of his annuity income to purchase a life insurance policy with a sum insured, equal to the capital invested in the annuity. Your annuity is reduced by a premium, which pays for this life assurance policy, to the benefit of your heirs. Such a plan normally comprises two separate contracts. The one is the annuity contract and the other a separate life insurance policy. The premiums that are paid in respect of the policy are not tax deductible by the annuitant and the proceeds of the policy on death is tax-free to the beneficiaries.

Joint and survivorship annuity.

An annuity product which ensures that your spouse, partner or dependant will have an annuity (fixed or variable) after your death. You select the income level your surviving dependant will receive (typically 75%). This is highly recommended for couples where only the one spouse has accumulated retirement savings and the two parties are close in age. This type of annuity pays out less than a single person annuity, as the longevity risk increases for the life assurance company. The annuity is based on the lowest age, so if there is a large difference between the two prospective annuitant it is not recommended unless there are sufficient other assets to ensure a comfortable retirement.

Enhanced annuities
In exceptional circumstances, you may qualify for an enhanced annuity if you can demonstrate that your life expectancy is restricted, such as a person that has cancer.

A living annuity
A living annuity is something I do not recommend as a stand-alone product for an investor that is not financially savvy. There are many reasons for this. The costs in the annuity can be greater than the return. These costs increase if you need to appoint advisors who may charge the maximum fees on top of the insurance and platform costs. You can circumvent the costs as you yourself can invest your retirement savings in single living annuity default portfolios run by funds, but you need to be aware of how to minimise fund fees, platform fees, maximise returns, and draw a sustainable income to keep the capital amount from running out. The annuity should be carefully structured to your needs, as it needs to be tax effective. Some counties do not allow you to move a living annuity from one insurer to another, should the insurer's performance become less than what you wish. Withdrawals are referred to as drawdowns in these annuities. In South Africa the minimum drawdown is 2.5% while a maximum drawdown is 17.5% of the capital invested. If you do not need 2.5% in income, the minimum drawdown could mean that you end up by earning income that you do not need and increasing your tax rate.

How does a living annuity work?

If we look at the sum of 1 million and put it into a living annuity, you have to look at the cost of fees and what you take out annually- this is called the drawdown. Your annual drawdown is normally increased by the cost of living (inflation) or the CPI (consumer price index). Each country will have a different inflation rate. The higher your inflation rate the more your money needs to work to bring in a higher return.

An example is with our 1 million. In this instance we drawdown 3% of this amount for ourselves, giving us an income of 30 000 per year, or 2500 per month. We have costs of 1.35% or 13 500 per annum. Our annuity will continue to perform for 23 years if we have an average 6% per annum, return on our funds and a 6 % inflation rate. Our drawdown in this case is 3%+1.35%= 4.35%.

For the person who retires at 65 it means they can live until age 88, at which point the annuity will start to fail. By age 92 they will have no more money left from that annuity. Remember the costs are 1.35%. What would happen if there 0.5% (5000) costs and the drawdown was 2.5% or 25 000 per annum? That annuity would last for 26 years at a 6 % inflation rate, giving us an extra 3 years, or until 91 years. In this annuity we would run out of capital by 96 years of age.

Inflation and costs are a major factor in the living annuity and some places charge up to 2.8 % in costs.

How do you work out the return on your money?

Simple!

Take the amount you start with in January which in our case is 1 million and divide it by the amount you have in December. Now if we have a 6% return this amount should be 1 060 000 or 60 000 per year.

1 060 000 /1 000 000=1.06.

Now just subtract the 1 because we want the percentage return on the sums and multiply by 100

(1.06-1) x 100=6%

6% may sound like a good return, but if inflation is running at 6% then your annuity is just keeping up its purchasing power, which is why it will run out. It will run out despite you having a drawdown of less than the return, because your drawdown and your costs are increasing by inflation. If you had a negative return for one year, this would worsen the situation.

How can you ensure the annuity remains positive?

In financial planning we use a process called diversification!

Diversification is when you do not keep all your eggs in one basket. Most managed funds do this in their prudential or retirement funds monies, by using what they call balanced or stable funds. These funds will invest in a basket of assets. The funds will own shares on the stock exchange, government bonds and cash. They may even invest in property. We will look at asset mixes in our section called “Making the money last”. In “Making the money last” we look at how you can mix and match the different retirement monies to ensure you are diversified and have a stable income in case dementia strikes.

The real danger in using a fund which protects the money from loss, is that the investor does not have enough exposure to growth assets, if we are to have an income that lasts, then we need to have a return that will exceed the inflation, costs and our drawdown.

Voluntary annuities
All the above annuities can be bought as voluntary annuities. That is an annuity bought with monies that do not have to buy a compulsory annuity. Most countries will give different tax rates on these annuities, due to a splitting of capital return and income. Every payment the person receives will have a portion of the original capital amount in it, while the interest is taxed as income.

Tom and Judy were shocked when his company gave him three weeks’ notice that he had reached the retirement age in the company. Tom had no idea that 60 years of age was his cut of date for the company. There was no counselling, just time for his co-workers to give him a dinner to say goodbye and then the last pay check.

Tom had always been a member of a retirement fund, but he had been retrenched 6 years prior to getting his present job. What he did not understand at the point of retirement, was that the retrenchment had taken his full lump sum tax free withdrawal amount. The company did not provide him with financial advice, but a representative of the provident fund contacted him. He discovered his full 6 years of saving in the provident fund was a paltry R 756 000. His previous company pension fund was R 5 million. Judy, was younger than Tom, but had been a housewife with a limited working career and had little in retirement savings. Tom approached a financial planner to help.

The couple initially asked for a living annuity to provide an inheritance for their children, but the return for a living annuity would be R 230 000 per annum, taking more than this would *severely deplete the capital and cause the annuity to fail. This amount was a far cry from his salary of R 650 000. In short he needed a two thirds reduction in living expenses.*

The adult children of the couple were consulted on the financial planner's advice. Together with the financial planner the family decided Tom should enter into a fixed annuity with his pension fund. This fixed annuity would return R 280 000 a year, increasing with CPI and was fixed for life. The annuity would also continue if Tom died before Judy for her life at 60% of the amount Tom was drawing. The provident fund money was invested in a living annuity to avoid tax. This would be drawn at a 4 % rate giving and extra R 30 240 per annum. This gave the couple a before tax income of R 310 240. A budget was entered into that ensured the couple would be able to live within the constraints. The budget allowed for Tom to maintain his life policy which would either serve as an addition to Judy's income or an inheritance for the children.

The couple had a large property as their only other asset. The option of selling the property was explored and rejected, as the resale value of the area was depressed and a sale would result in the couple having to use capital for a retirement home. The property was able to be used more productively, if they kept it and changed it, to allow it to work for them.

The house was divided to create a flat which was rented out. This was estimated to bring in an extra R 3 500 to the couple with very little impact on their life style, in the rest of the property. The cost to convert the flat was R 130 000 and this was funded from existing savings. A tenant was sourced from the couple's church.

The use of a professional had increased Tom's income and decreased his costs. This had been done at a lump sum fee of R 6 500 for the nine hours it took the professional to determine the situation and out in the solutions. Tom also received advice on a more cost effective medical scheme and his short term insurance needs which reduced the lump sum fee as the broker received commission for these purchases. Tom did not wish to pay a management fee for the living annuity and opted for the lump sum fee, with regard to this advice, although the financial planner would send via email, investment updates and a newsletter as Tom was now a client. The children, by being part of the negotiation, were aware of the situation and agreed to put funds toward their parent's upkeep, these funds would be kept in a tax free savings account and only accessed when required. This was to provide a safety net, if the couple ran into medical situations or needed frail care. The option of frail care insurance was discarded, as the children felt they could self -insure for this eventuality.

Tom and Judy are managing on the budget. The flat income allows them to take regular holidays in their caravan, while the tenant takes care of their animals.

Why must you exercise caution with annuities?

The correct choice of annuity is really important, as the temptation of taking the higher initial income from a level annuity could prove to be unwise, particularly considering our increased life expectancy

The fixed annuity will cease on death unless we have taken out some form of insurance (guarantee). The fixed annuity may be taken as a level annuity which is the same amount for the rest of your life. Great if you have no inflation or intend to die in around 10 years as you will come out better on the level annuity than an escalating one.

I personally prefer escalating annuities as we are living longer, but the choice is the annuitants. I would want an annuity escalating by a factor such as inflation. Again try and match expenses to this income if possible. The fixed or conventional annuity means there is no choice of portfolio- the investment house will take care of that.

In any type of annuity the best advice is shop around. If you do not understand the product find someone who can explain it to you. Some products are very complicated and linked to wellness targets and interlinked with certain performance criteria. Insurers certainly have not become rich by letting us understand what they do.

An income for life is a major plus for budgeting – you know exactly what you are going to get in advance. With life annuities, pensioners carry no longevity or investment risk, as the initial pensions and increases are guaranteed for life, and will never decrease. These annuities also release pensioners of the stress of having to make their own investment choices. This is especially important when cognitive ability starts to decrease during old age. A life annuity is therefore advised for those people who may not have the discipline to keep withdrawal rates down, or persons that can no longer make their own decisions. Joint annuities are valuable for those with significant others to take care off, but may be counter indicated if the age difference is too great between the couple.

The correct matching of annuities on an income need, can reduce the need to rely on families, friends, charities and government to help make ends meet during retirement. Those who are lucky enough to have spare cash or need a living annuity will need to understand how to make the income last.

A living annuity can be commuted to a fixed annuity, if interest rates are low at the point of retirement. Using a combination of the different annuities may be more suitable for a person than choosing a single annuity, subject to their personal circumstances.

Chapter 3: Business in retirement

While busy with our careers, we tend to have a higher concept of our importance to society. Work is a meaningful act because it creates value (not only monetary). When we stop work we lose that value and this can lead to depression and isolation. Often a retiree cannot continue to work, as society does not value the contribution an older person can make. Many retirees take on lowly paying jobs as a result of this attitude, because of need or sheer boredom. Retirees have immense skills, born of experience, fortitude and intelligence. They have simply retired, not lost their brain, but circumstance may make them feel otherwise.

People in 50-60s start businesses at twice the rate of those in their 20s. Necessity normally drives this need. Entrepreneurship rises in recession and “lifetime” employment when over 50, declines in the recessionary period.

People past retirement age do not necessarily have to carry on in the same jobs as before. In Japan pensions are small and lots of people are still working in their later 60s and even 70s. Companies like Hitachi have found ways of re-employing staff after retirement—but in a different capacity and, significantly, at lower pay. Companies have asked their high skills employees to work for shorter hours or to consult. Some retailers such as Wal-Mart or Britain's B&Q, and caterers such as McDonald's, have started hiring pensioners because their customers find them friendlier and more helpful. In addition skills shortages has caused companies to bring back older workers. A retirement plan in which the future pensioner decides to upskill in an area of skills shortages is not the worst idea one can have.

Ernst is an engineer who consults to mines. At his retirement he has upskilled on project management and started a new business in which he contracts to countries such as Mali and Ghana. This allows him to oversee new engineers with the benefit of his experience in occupations where experience counts, but without the drawdown of a younger person who would be hesitant to impart their knowledge because of the danger they would then damage an incoming income stream.

Starting a new business in retirement

Pensioners can also consider starting their own business. New business can be a risky business, for the first time business person and catastrophic for the pensioner! Many pensioners risk all the retirement provisions into such a vehicle and loose it when the business fails. However a small business can also give great comfort and bring in some spending money. The same rules apply to a retiree business as to normal business. Think, do an analyses, think again and only then act.

The retiree may look at using their hobby as a business.

Tandy, loves her sewing hobby and wants to open up an embroidery service, to bring in extra money during her retirement. She has a domestic embroidery machine, but feels she would need a bigger industrial machine. She will require a loan for this machine. She has done embroidery as a favour to her friends and she thinks there is a market.

How should she go about this process of creating a business?

She would need to create a Marketing Plan. The marketing plan is a highly detailed, heavily researched, document that describes the benefits the customer gets when using or buying the product.

It will detail her:

Market: Where her products or services are sold.

Marketing: The method of promotion and/ or selling of her service.

Market Orientation: gives the business strategy whereby her company focuses on meeting the customers' needs and wants.

Market Sector: Competing businesses, which produce or buy similar goods and/ or services which she will offer.

It includes the 4 Ps of Marketing

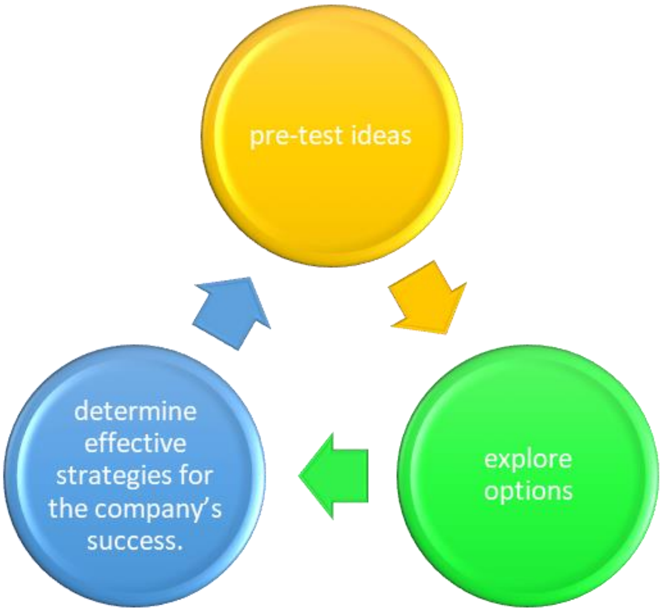
Product: what is she selling?

Price: what will she charge for her time and the material used?

Place: Where will she operate and where will her market be?

Promotion: how will she make herself known?

Tandy should then run a test drive using her domestic machine to accumulate the figures and determine if the demand will require an industrial machine,



If her product sells she can then move onto the next phase of her business plan and apply for a loan.

Tandy determined she would first be advised to use her existing machine, doing private jobs. Her name became known and she started to do small lots for companies. She bought a second hand industrial machine and makes a comfortable income. She uses her domestic machine and has got her friend involved in helping with larger orders.

By starting small and containing costs Tandy was able to supplement her pension. Tandy had a skill and a machine, which puts her into a fortunate category. If Tandy had to get a loan to buy her equipment, her business may not have been successful. A business needs cash to survive, and loans eat cash reserves as they need to be paid.

Some pensioners have an external interest or may have been helping with the grandkids. As a result they could decide to make this into their retirement business.

David has a great interest in his grandson and the school he attends. David went to the same school as did his father before him. His grandson has become passionate about rowing and David has been able to accompany him to the rowing heats. David is very hands on and loves DIY. When the opportunity came to buy a rowing scull for his grandson, for an affordable price due to the work needed, David decided to restore the scull as a project.

David enjoyed restoring his grandson's rowing scull. The school after seeing the result asks him to undertake their rowing boat maintenance. David suggests that he either gets remunerated per hour of work, or on a contingency of sixteen hours per month. The school will pay for any material he requires.

The school obtains his services on this contingency basis, which means they get an enthusiastic member of the team, David enjoys his work and is frequently at the boatsheds repairing the boats. He enjoys interacting with the students.

Although David is doing a service for a school, he has ensured he is not to be abused. It is very easy for a pensioner to agree to voluntarily take on work for no compensation. Such a situation can lead to the person not being treated with the same respect and consideration a salaried employee would receive.

In section 3 we will explore the life after retirement and how you can now spread those wings. However we have to also look at the dangers you will face.