USAF
Universiteit Stellenbosch AFTREDEFONDS | Stellenbosch University RETIREMENT FUND

NUUSBRIEF | NEWSLETTER September 2017

UNIVERSITEIT STELLENBOSCH UNIVERSITY

CONTENTS

Chairman's Report

I have pleasure in looking back on the past few months of 2017 and giving feedback on what has happened in the Fund during the past year.

In 2016 the Board of Trustees reviewed the offshore asset managers. The improvement in the offshore investment managers' returns resulted in a remarkable improvement in the returns on the Growth Portfolio compared to the agreed benchmarks, in spite of uncertain economic and political conditions.

The implementation of the in-fund living annuities resulted in the existing investment strategy and the lifestage investment strategy being revised as from 1 January 2017. More options are now offered to members from age 53 in order to align their investment strategy prior to retirement with the type of annuity they would like to buy at retirement. More information on the types of annuity options at retirement follows later in the newsletter. We would like to remind you again of the in-fund living annuity and the deferred retirement options offered by USAF.

Both the audited financial statements and actuarial valuation for the year ended 31 December 2016 were approved by the Board of Trustees and submitted to the Financial Services Board. The auditors issued an unqualified audit report and the actuary confirmed that the Fund is financially sound.

A smartphone app will be rolled out in due course. More information on this will be provided in the next newsletter.

Regards

Adv. F.A. du Plessis
Chairman

The 31 December 2016 Financial Statements and Actuarial Valuation

Financial Statements

The audited financial statements for the year ended 31 December 2016 were submitted to the Audit and Risk subcommittee of the Board of Trustees in June 2017. USAF's external auditors, PwC, issued an unqualified audit report. At recommendation of the Audit and Risk subcommittee, the Board of Trustees approved the financial statements and submitted them to the Financial Services Board before the deadline of 30 June 2017.

Actuarial Valuation

An actuarial valuation is performed annually, once the audited annual financial statements as at 31 December (the fund year-end) have been received, in order to determine the financial soundness of the Fund. The 31 December 2016 actuarial valuation was presented to the Board of Trustees in August 2017.

In the valuation report the actuary confirmed that USAF was in a sound financial position at a 100.05% funding level. The valuation report was approved by the Board of Trustees and submitted to the Financial Services Board.

Fund investments

The table below provides a summary of the Growth Portfolio returns over various periods to 30 June 2017:

Period	Growth Portfolio	Inflation	Inflation plus 5%	Peer group median*	Peer group top quartile**
3 months	0.45%	0.98%	2.21%	0.44%	0.86%
6 months	4.08%	3.11%	5.58%	3.29%	4.02%
12 months	5.98%	5.44%	10.44%	3.37%	4.50%
36 months	7.43% p.a.	5.40% p.a.	10.40% p.a.	6.27% p.a.	6.68% p.a.
60 months	14.13% p.a.	5.68% p.a.	10.68% p.a.	11.88% p.a.	13.29% p.a.

** The peer group median is the investment manager that performed in the middle of its peer group. This provides an indication of the performance of other retirement funds over these periods. The peer group benchmarks are derived from the Alexander Forbes survey.*
***The peer group top quartile constitutes the investment managers that performed better than three-quarters of their peer group.*

It is encouraging that the Growth Portfolio returns outperformed the top quartile peer group over all the measurement periods longer than 3 months. This is largely the result of an improvement in the returns achieved by the offshore investment managers. However, you are advised not to pay too much attention to short-term returns - rather focus on the longer-term returns.

For further information on all the returns achieved by the underlying portfolios, please visit www.retirementfundweb.co.za.

Changes to the investment strategy and the lifestage strategy

With the introduction of the in-fund living annuities the Board of Trustees revised the investment strategy as from 1 January 2017.

All members are invested 100% in the Growth Portfolio until age 53.

Four additional investment portfolios have been made available to members from age 53 in order to align the investments of these members near retirement with investments suitable for annuity products.

From age 53 the following investment options are available to members

- Growth Portfolio
- Aggressive Absolute Return Portfolio
- Conservative Absolute Return Portfolio
- Portfolio offering hedging against interest rate fluctuations
- Capital Protection Portfolio

The Aggressive Absolute Return Portfolio and the Conservative Absolute Return Portfolio are suitable for the in-fund living annuities, as well as for the purchase of external living annuities (outside the Fund).

The Portfolio offering hedging against interest rate fluctuations is suitable for the purchase of external guaranteed annuities at retirement.

The Board of Trustees recently decided also to offer a Shari'ah investment portfolio option to members who would like their fund credit to be invested in accordance with the principles of the Islamic religion.

The new lifestage strategy

The Trustees also revised the asset split and phase-in period of the lifestage strategy to be more suitable for the in-fund living annuity strategy. Hence the Board of Trustees decided to extend the phase-in period from three to **six years**.

According to the new lifestage strategy, with effect from 1 January in the year of the member's 60th birthday, the full fund credit is to be transferred from the Growth Portfolio to the Aggressive and Conservative Absolute Return Portfolios in equal portions, via 25 quarterly transfers, resulting in the fund credit being held in equal portions (50/50) in the two Absolute Return Portfolios.

Members will still be able to exercise options outside the new lifestage strategy, and now they have more options to choose from.

Annuity options at retirement

At retirement you are faced with a number of decisions you will need to make. With so many different annuities (pension options) available, this could be a daunting task. However, it does become easier if you understand the available options, the factors that influence the size of the monthly pension, and the differences between the types of annuities. Another important aspect is understanding the risks attached to the different annuities.

What are the risks attached to annuities?

The most important risks associated with the different annuities available to members at retirement are the following:

- Longevity risk - the possibility that you will outlive your money;
- Investment risk - the possibility that the investment return earned will be less than what is required to provide you with the necessary pension income; and
- Inflation risk - the possibility that your pension income will not be able to keep up with your living expenses.

What are the different types of annuities?

Annuities can be split into two categories, each with a number of options which include various features.
These two categories are called:

1. Guaranteed or life annuities, and
2. Investment-linked annuities.

1. Guaranteed or life annuities

A guaranteed or life annuity is an insurance policy or contract between you, the member, and an insurance company. USAF pays a capital sum to an insurance company of your choice in exchange for a monthly income (based on certain agreed conditions) that is guaranteed until your death. These conditions are agreed on right at the start and cannot be changed later. The longevity and investment risks, as indicated above, are transferred to the insurance company and the pension will be paid until the pensioner dies. However, like all guarantees, this guarantee comes at a price. The cost of additional security, for example with regard to future increases, will have an impact on the monthly pension payable to you.

Types of guaranteed or life annuities are the following:

Escalating guaranteed life annuity – the pension payments will **increase at a fixed rate** per year.

Level guaranteed life annuity – the monthly income is paid for life and will **never increase**.

Inflation-linked life annuity – the pension will **increase in line with inflation** on an annual basis.

With-profit life annuity – the pension will **increase annually depending on the investment returns earned** on the investment portfolios in which it is invested and the initial purchase rate.

These types of annuities may be structured as *single-life annuities*, which means that only the pensioner is insured or provided for. However, a number of extra conditions may be added, such as providing for a spouse's pension upon the death of the pensioner so that the surviving spouse will have a pension for life. This is called a *joint-life annuity*.

As always, you are advised to consult an accredited financial adviser who will assist you through the process.

Your adviser will obtain annuity (pension) quotations from various insurers and advise how much you can expect to receive as a monthly pension, according to the various insurers' quotations. The monthly pension amount will depend on the capital sum available, as well as a number of other factors.

What are the most important factors that determine the monthly pension amount of a guaranteed or life annuity?

In the table below we take a look at the main factors and how they affect the size of your monthly pension amount:

Your capital amount	This is the portion of your fund credit that is used to buy the pension. You can use your full fund credit or any part thereof to purchase your pension. The bigger the capital amount, the bigger the initial monthly pension will be.
Your gender	Research has shown that females are likely to live longer than males and therefore their pension has to last longer than that of a male. Therefore the initial monthly pension income of a female will often be less than the monthly pension income of a male, which is expected to be paid for a shorter period.
Your age	Determines your life expectancy – i.e. how long you are expected to live. The older you are when you buy your pension, the bigger your initial monthly pension will be.
Your chosen guaranteed period	How many years you want your pension to be guaranteed to be paid for. If your guaranteed period is 10 years and you pass away 5 years after you retire, your monthly pension will be paid to a beneficiary of your choice for the next 5 years. Examples of guaranteed periods are 5, 10, 15 or 20 years. The longer the guaranteed period you choose, the smaller your monthly pension will be.
Your chosen future increase	Whether you require annual pension income increases, and the level of these future increases. If you do not select a future (inflationary) increase your pension amount may not keep pace with your living expenses. This may become a problem as the buying power of your pension will reduce year by year – which means you will be able to buy less with your monthly pension. The bigger the future increase selected, the smaller your initial monthly pension will be.
Your spouse's pension	Whether you require a pension to be paid to your spouse if you pass away before your spouse, and whether your spouse's pension should be equal to your pension or a portion (percentage) of your pension. This will also have an impact on the initial pension amount. A spouse's pension is usually equal to 50% of your pension at the time of your death.
Interest rate movements	Certain options are sensitive to interest rate movements and can differ by about 4% for every 1% movement in interest rates.

2. Investment-linked annuities

An investment-linked annuity is an investment product in which the income is not guaranteed. Pension payments depend on the performance of the underlying investments in which the pensioner is invested. However, **if managed well** this type of annuity could provide a higher level of income during your retirement.

The pensioner "draws down" an agreed amount from the investment each month by taking a small percentage of the investment as a monthly pension. In terms of current legislation a pensioner may choose an income of between 2.5% and 17.5% of the capital invested. The chosen percentage may be changed once a year. Thus this type of annuity allows for greater flexibility with regard to income.

As a member you carry the *longevity* and *investment risks*. Therefore there is a risk that your money could run out if you draw too much too soon. However, should you pass away, all of the remaining capital will be payable to your beneficiaries. All investment returns from the capital you invested will be allocated to you.

What are the differences between the different types of annuities?

The table below shows the differences between the most common annuity or pension options used by retirement fund members:

	Increasing guaranteed life annuity / pension	With-profit annuity / pension	Investment-linked annuity / pension
Features	• At retirement the member decides on a rate of increase (the higher the rate of increase, the lower the initial pension will be). • When the pension is purchased, the member has a choice regarding a minimum guaranteed period and a spouse's pension option.	• The pension is purchased at a fixed rate and will increase by the investment returns declared, less the rate at which it was purchased. The higher the purchase rate, the higher the initial pension but the lower future increases will be. • When the pension is purchased, the member has a choice regarding a minimum guaranteed period and a spouse's pension option.	• The pensioner obtains an investment account and chooses the portfolio(s) in which the retirement capital will be invested. • The pensioner chooses the monthly pension, which must be between 2.5% and 17.5% of the capital amount. The rate chosen by the pensioner may be changed once a year, based on the capital amount at year end. • A pensioner may nominate a person (e.g. his/her spouse) to receive the balance of the capital which the nominee may choose to receive either as a lump sum or as a monthly pension (depending on the remaining capital amount)
Risks	• Future rate of inflation is unknown. For example, a member could select an annual pension increase of 5%, whereas the inflation rate increases by 10%. • Low interest rates at retirement will mean monthly pensions will cost more than when interest rates are high. • At retirement the member selects options that cannot be changed, which means the pension is not flexible.	• In times of poor investment performance pension increases could be low or might not be granted at all.	• The pensioner carries the full investment risk. • Investment decisions are important and volatile investment markets could result in the capital decreasing. • If the pensioner withdraws a monthly pension at a higher rate than the investment return earned on the capital, the capital will decrease and will probably be depleted sooner than expected.
Benefits	• The pensioner has certainty about future pension payments as the pension is guaranteed for life. The annual increase as well as what happens in the event of death, etc. is agreed upon upfront.	• Since the pension increases are linked to the investment returns declared (less the rate at which the annuity was purchased), the pension may, to some extent keep up with inflation. • The monthly pension will never decrease.	• A pensioner supported by sound investment advice could retain control of the investment decisions regarding the retirement capital, with greater flexibility with regard to the annual pension. • The pensioner chooses the level of annual pension increases - within the guidelines set by the authorities.

There is no one-size-fits-all annuity (pension) type that will work for every situation and for every pensioner. The ideal pension will depend on the size of your fund credit, your personal needs as well as the current economic climate.

Just like the premier economy class meets more than one need of passengers by offering a more affordable option for more legroom, hybrid and composite annuities meet the needs of retirees by offering access to capital and good returns, and protection against risks.

Composite annuities are becoming a popular option in the market, with the following versions:

- A living annuity, which is phased in over a period in a guaranteed annuity.
- A living annuity, which is purchased together with a deferred annuity at inception.
- A term annuity, which is purchased for the first 5-10 years. After that, income is received from a living annuity.

It is very important for members to choose a retirement product that best provides in their needs. This choice should preferably be made in consultation with an accredited financial adviser.

Did you know?

R1 million invested to purchase a **single-life annuity** (no spouse's pension at the death of the pensioner), with annual inflation-linked increases and no guaranteed term, will:

provide a 65-year-old **male** with an initial pension of **R6 128** per month, and

provide a 65-year-old **female** with an initial pension of **R5 480** per month.

Females initially receive a smaller pension as they have a longer life expectancy.

In-fund living annuity option

Since 1 January 2017 USAF offers in-fund living annuities that provide you with a seamless transition from contributing member to pensioner. If you elect to participate in the in-fund living annuities you don't have to leave the Fund on retirement. The amount you saved for retirement as a member of USAF and that is not taken as a cash lump sum, is used to buy a monthly pension. USAF now offers a default as well as a customised option for living annuities.

The default option represents the Board of Trustees' view of the best option for the average member. The withdrawal rates are fixed and no investment choice is allowed.

In contrast, the customised option offers investment choices and more flexibility in terms of withdrawal rates.

A pensioner is allowed to switch between the default option and the customised option. In-fund pensioners may also switch to an external solution at any time after retirement.

In both the default and the customised option you benefit from competitive administration and investment fees. Asset management and administration costs are expected to be less than 1% p.a. of assets (VAT included), which compares very favourably with costs in the individual market. In addition, the trustees of USAF are responsible to ensure that the withdrawal rates from the in-fund living annuities are sustainable, and they will assist you in considering other alternatives from time to time. The trustees have access to professional advice to assist them with the governance and management of the in-fund living annuities. The option for individuals to continue to receive financial advice from the panel of approved service providers is also available.

Deferred retirement

The decision to retire early can have an impact on your lifestyle after retirement and should be considered carefully. USAF offers you the opportunity to remain a member of the Fund when you retire from employment with the University, and by doing so to increase your retirement money. If a member defers retirement from the Fund for five years, it could have a significant impact on the value of the monthly pension at retirement.

Remember that you have a choice to defer retirement from the Fund on retirement at normal retirement age or on early retirement. How does it work? If you opt for deferred retirement when you retire from employment with the University, your fund credit will remain invested in the Fund while you obtain income from another source. You can decide when you want to retire from the Fund at a later stage, or rather when you can afford to do this.

The University has also given consent for employees who opted for deferred retirement and are re-employed on a temporarily basis after retirement, to continue to make contributions to the Fund. However, the employer will not allow these contributions as a tax deduction.

On your death subsequent to exercising the deferred retirement option, your dependants will only receive the accumulated fund credit in the Fund, as the insured death benefits will have ceased on the date of retirement from the University.

The monthly administration fees will be recovered from your fund credit, and you will still have access to your fund information via the Fund's online portal, Retirement Fund Web until you eventually retire from the Fund. By opting for deferred retirement you will still benefit from the economies of scale applicable to the Fund's administration and investment fees.

From the age 55, members have the following options when considering retirement from US:

• Deferred retirement to maximum age 70
• In-fund living annuity
• Annuities outside of the Fund
• Cash.

If you are interested in exercising the deferred retirement option, you may contact Mr Peter Kirsten of the Remuneration and Benefits Department for more information.

Financial advice

You are reminded that USAF offers a financial advice service to members that is free of charge. Members aged 53 and older have access to this service. In particular, members who are considering early retirement and want to exercise individual investment choice, are encouraged to make use of the advice service.

The panel of preferred service providers comprises:

Alexander Forbes Financial Planning Consultants:	+27 (0) 21 809 3750 / wesselsw@aforbes.co.za
Efficient Wealth:	+27 (0) 21 914 8030 / martin@efw.co.za
Finfocus:	+27 (0) 21 861 7000 / usafadvies@finfocus.co.za
Graviton:	+27 (0) 21 883 9192 / arissik@gravitonwm.com
Sanlam Financial Advice:	+27 (0) 21 947 6025 / karl.parks@sanlam.co.za

USAF will pay for two consultations with one of the preferred service providers.
The first consultation may be scheduled any time from age 53, and the second one on retirement. Using the benefit is easy – just follow these steps:
1. Select a service provider.
2. Contact Human Resources (Charné Pool at +27 (0) 21 808 9271 / charnep@sun.ac.za) to obtain a consultation voucher.
3. Make an appointment with your chosen service provider and take the voucher as proof that you are entitled to use the service.

Important contact details

If you need more information on USAF you may contact the Remuneration and Benefits Department or the benefit consultant. Please contact the principal officer if you have any complaints about USAF.

Principal Officer	**Japie Kotze** t. +27 (0) 21 808 2754 f. +27 (0) 21 808 2484 e. jjsk@sun.ac.za
Benefit Consultant	**Alfreda April** f. +27 (0) 21 912 3316 e. alfreda@simekaconsult.co.za
Remuneration and Benefits Department	**Peter Kirsten** t. +27 (0) 21 808 3740 f. +27 (0) 21 808 2484 e. pkirsten@sun.ac.za
Pension Funds Adjudicator (PFA)	e. enquiries@pfa.org.za Members may contact the Pension Funds Adjudicator if their complaints have not sufficiently been dealt with by the Fund. Please consult the PFA's website (http://www.pfa.org.za) for more details.