

01/05/2001

Don't let the sun set on your twilight years

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THIS WILL be my final offering of Compass for Malaysian Business. It is with a heavy heart that I need to end what has been an exquisite relationship. Escalating work and professional development commitments have meant that something had to give. After enormous contemplation, I find that I must relinquish the bulk of my ongoing writing assignments.

It is fitting that the closing subject of this series, which began on June 1, 2000, is retirement (in general) and the use of your Employees Provident Fund (EPF) money (in particular).

There was a slight storm in the proverbial teacup a while back over the government's decision to cut employees' contributions from 11 per cent to nine per cent of gross salary - for one year. A quick analysis showed me that about half of the RM3-billion stimulus package announced about a month ago came from the projected increase in consumer spending arising from that two percentage point cut over 12 months.

But in response to surprisingly vociferous outcries from consumer groups and unions, the government effected a `U' turn. Prime Minister Datuk Seri Dr Mahathir Mohamad went so far as to say that it is now entirely up to individuals to decide if they want to reduce their contributions or not.

Personally, I think returning a portion of self-responsibility in this matter to the populace is a wise move by the authorities.

As for the EPF decision, I applaud the loosening up from a laissez faire policy standpoint. But trust me when I say that two percentage points over just 12 months isn't that big a deal. What is far more important is how you and I manage our growing EPF funds in the years or decades ahead before we hit 55.

What follows is my personal take on some of the options the EPF Board, usually under government instruction, has made available.

Just to make sure each of us is on the `same page', here is a rundown of the current situation:

Each EPF member has three EPF accounts, Account 1, Account 2 and Account 3. Each month, when contributions are made, the money is split three ways, with 60 per cent going into Account 1, 30 per cent into Account 2 and 10 per cent into Account 3. These accounts are respectively dedicated to funding retirement; housing, higher education (degree-level only), computer purchase and early withdrawal at 50 years of age; and medical expenses. (A recent development allows funds from all three accounts - starting with Account 1 and moving down to Account 2 and then Account 3, if necessary - to purchase annuities from authorised insurance companies.)

By far, the best option I know of - one that I have taken advantage of for myself, and which I have helped some clients put into effect for themselves - is the Member Investment Scheme that allows periodic partial withdrawals for unit trust investments. I will return to this later.

The conventional annuity scheme that the EPF Board has made available through six local insurance companies is - in my opinion - an option that ideally suits one category of Malaysian retirees: Those incapable of personally handling large sums of money.

Unfortunately, these people seem to form the bulk of Malaysian workers, at least based on findings that the average 55-year old EPF contributor uses up all his EPF funds within a mere three years of official retirement.

Obviously, such individuals should actively scrutinise the annuity

scheme, which buys participants a steady future stream of post-retirement income in exchange for however much of their EPF funds they are willing to pay for that service. Yet, if I am painfully blunt - at the risk of offending some parties - every single client I have taken on in my own financial planning practice does not fall in that category. For I have found that a large part of helping people with their financial planning needs revolves around the triple necessities of:

1. Educating them,
2. Raising their general awareness of mathematical realities, and
3. Managing long-term expectations of sustainable returns.

It has been my experience that those Malaysians sophisticated enough to buy into such a long-term process of taking personal responsibility - with or without the aid of appropriate professionals - will not be best served by the annuity option. At least, as it is currently structured.

I believe that in the majority of cases, the best use of Account 2 money is to retire mortgage debt as fast as possible. Using the money to fund a child's tertiary education is a close second. I applaud the government's attempts to raise the level of computer literacy, but I don't like what I have seen and heard about the abuses concerning this withdrawal option.

Returning to the viability of using EPF money to retire a primary mortgage, I maintain my enthusiasm even in the face of the recent flurry of competitive activity between our banks that has made available basement rates to both new house buyers and mortgage switchers.

Most people can clearly understand the sense in using money growing at six per cent (the latest EPF dividend rate) to retire debt that may be costing between 7.4 and nine per cent. But why do I maintain my position that Account 2 money should also be used (wisely) in situations where banks are only charging three to four per cent? Three reasons: