Distributing long-term saving policies in a low-saving environment

Lessons from South Africa

Rob Rusconi | Independent Actuary

IAALS Colloquium, Barcelona, October 2017

Summary

- Individual long-term saving product provided poor value for money
  - particularly in the event of early termination or any form of policy change
  - contributed to by high levels of sales commission
- The regulator faced the challenge of implementing widespread change
  - while retaining consumer confidence in the industry, and
  - encouraging continued participation by suppliers and intermediaries
- A number of lessons may be applicable to other jurisdictions

South Africa is a middle-income country

- The simple statement hides considerable complexity
- South Africa combines at least two economies
  - a sophisticated and wealthy middle-to-upper class, and
  - high levels of poverty and unemployment
- Inequality levels are amongst the highest in the world

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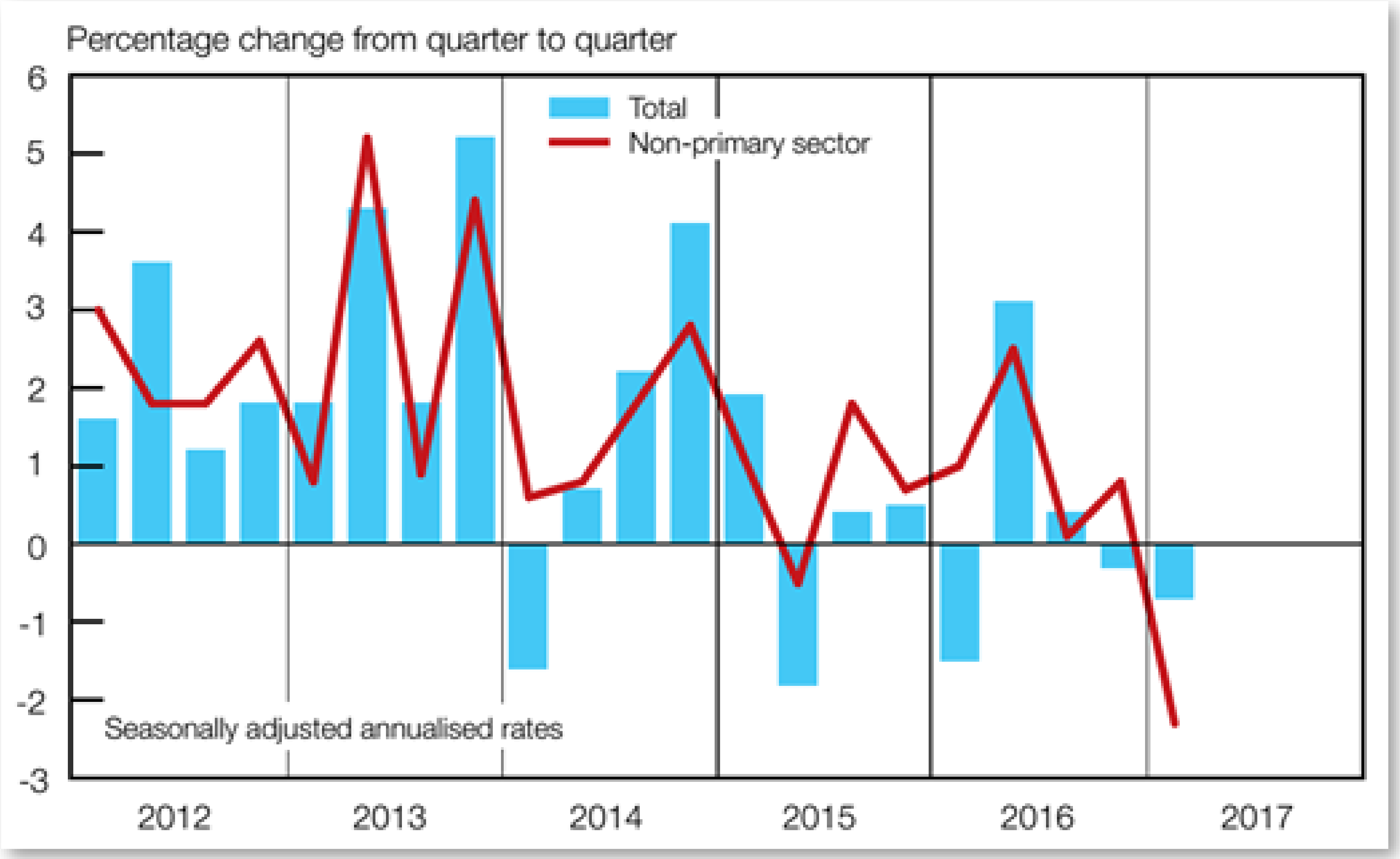
Percentage change from quarter to quarter
6
5
4
3
2
1
0
-1
-2
-3
Total
Non-primary sector
Seasonally adjusted annualised rates
2012
2013
2014
2015
2016
2017

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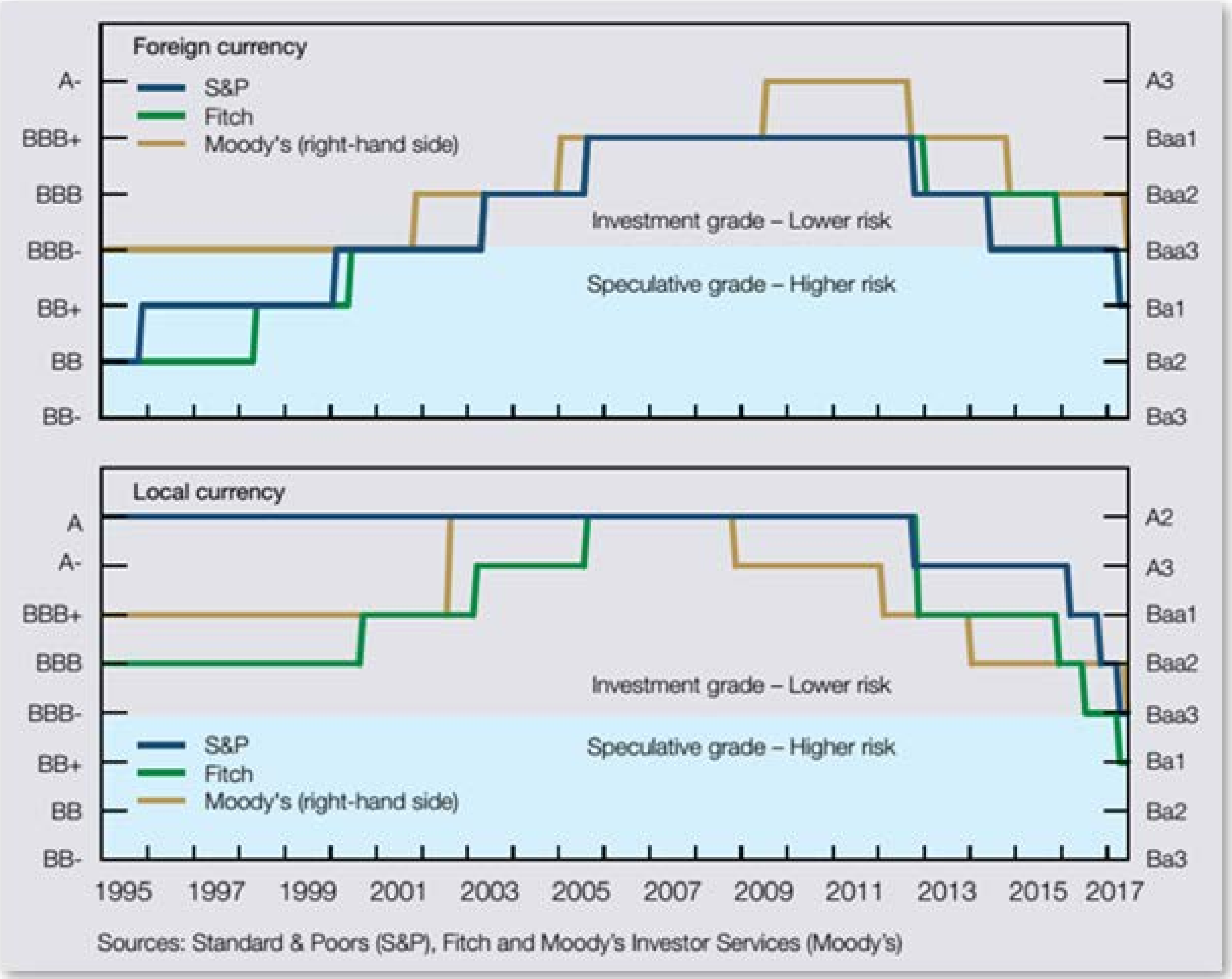

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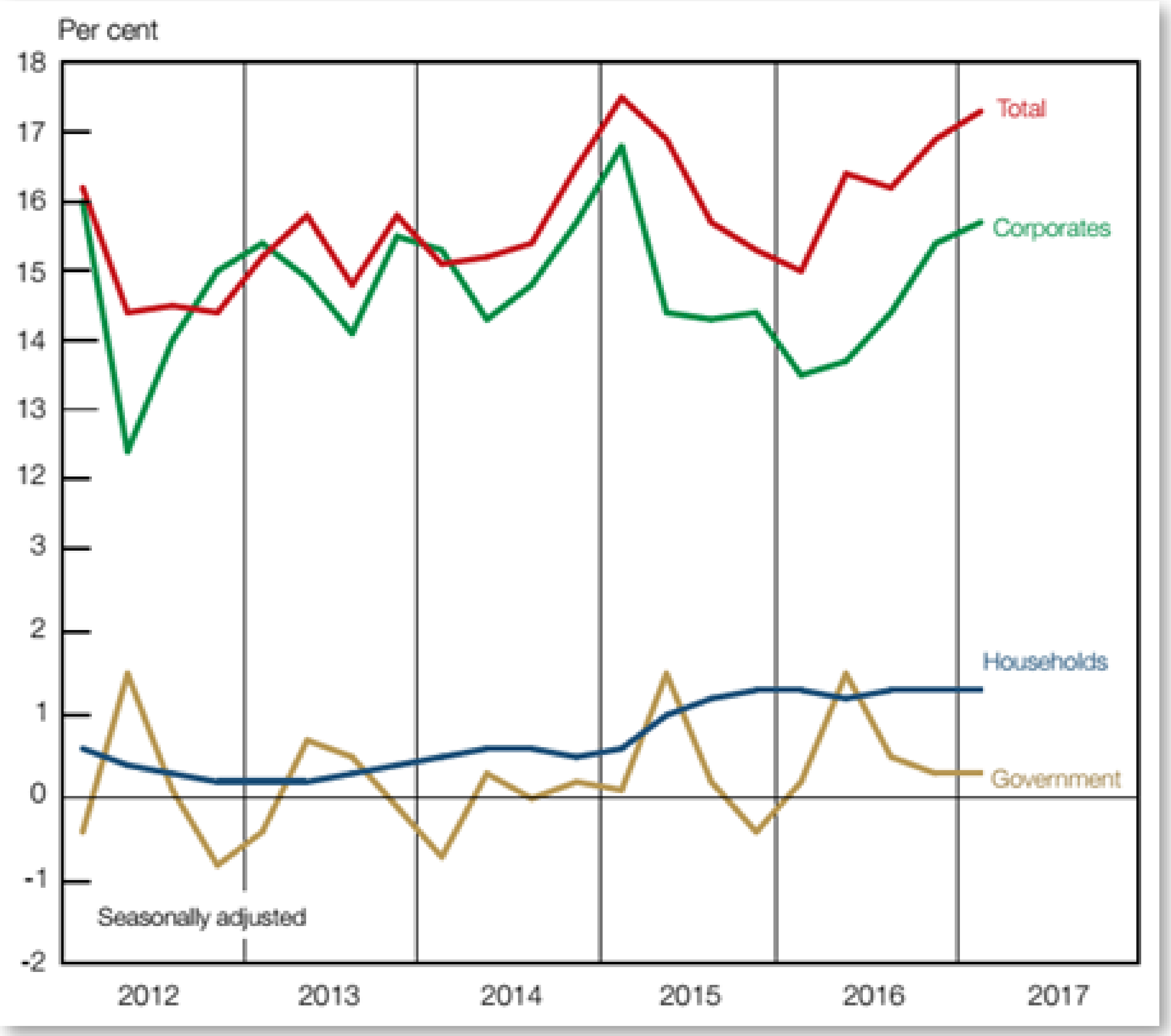


Pension system

- Pillar Zero, non-contributory pension
  - Means-tested, but in practice nearly universal
  - USD125 monthly pension generous by regional standards
  - Highly effective means of supporting recipients and families
  - Costs 1.72% of GDP, not coming down
- Pillar One, mandatory centralised contributory system
  - Not in place in South Africa, despite considerable discussion

Pension system

- Pillar Two, mandatory decentralised contributory system
  - No government mandate to participate
- Pillar Three, voluntary retirement saving
  - In most countries, a supplementary benefit
  - In South Africa, this is the heart of the system, supported by tax incentives
  - Occupational arrangements, of various sizes
  - Multi-employer schemes, mostly established by for-profit arrangements
  - Collective schemes offered by life insurers and collective investment houses
  - All subject to the same laws and principles of fiduciary oversight

Pension system

- Pillar Four, informal, household and other non-cash transfers
  - Play a big part in supporting South Africa’s elderly
  - Formal saving for retirement for many not a priority
- ILO points out South Africa as different to many
  - No earnings-related income benefit
  - Inadequately comprehensive social security system

High levels of dependence on voluntary saving arrangements

Supply side for individual long-term saving

- Strong prudential leaning in the regulatory environment
- Product space traditionally dominated by insurers
    - Typically bundled with risk cover
    - Supported by regulated commission scales
    - Part of a move to general financial services, though
    - Assets under management typically are the key measure
- Specialist investment houses slowly entering the market
    - Distribution is challenging

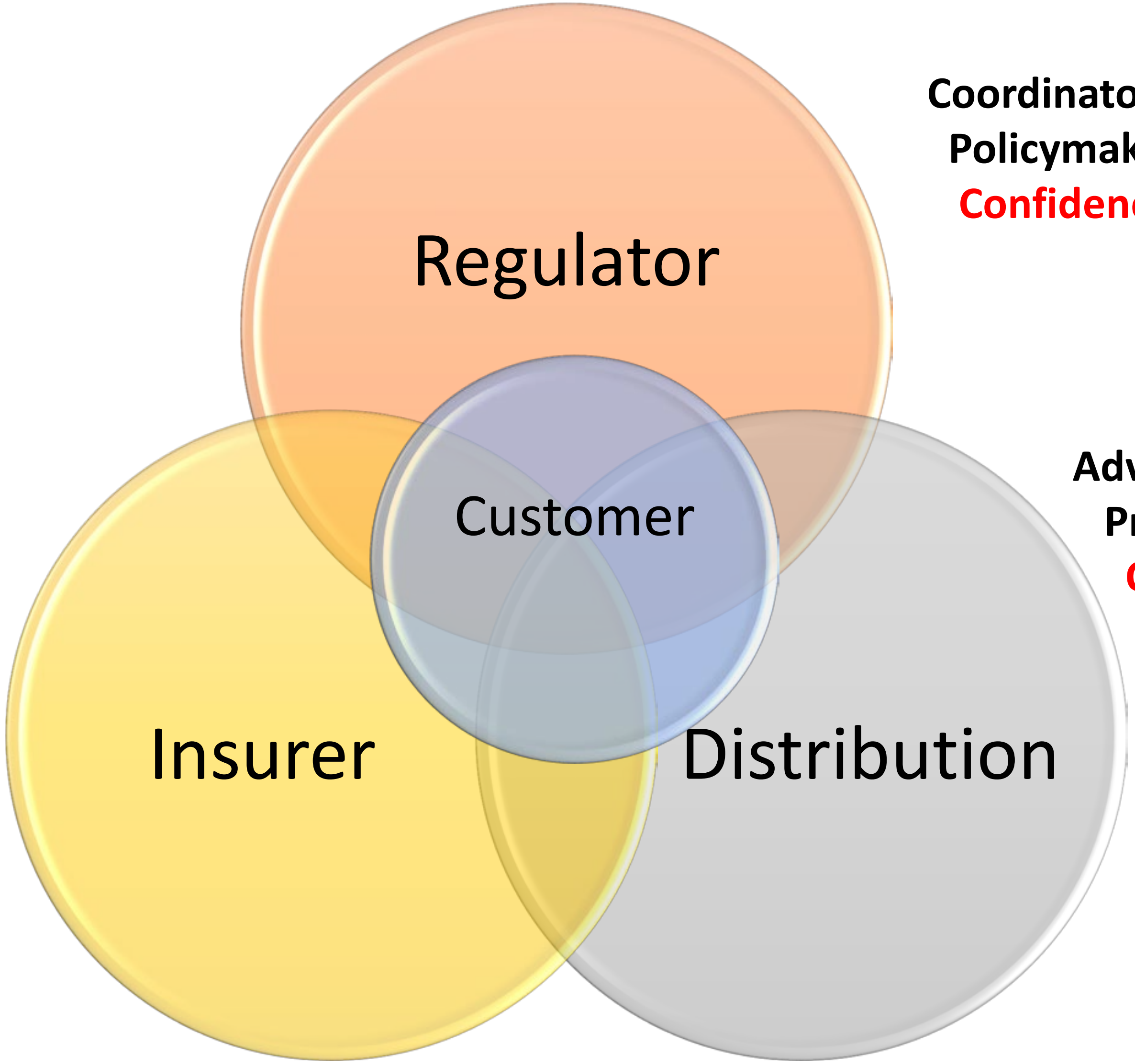
Describing the problem

- Historical product design
  - Long-term insurance arrangement
  - Under the structure of a retirement fund, with associated tax benefits
  - Sometimes bundled with other benefits
  - Typically inflexibly structured, with
  - Insurer freedom to respond to customer change requests
- Sales expenses high
  - Commission payments typically the highest contributor

Describing the problem

- Adverse publicity
  - Evidence of high charges in the products
  - Ombud rulings regarding charges on termination or product changes
  - Concerns over inadequacy of disclosure
  - High levels of public pressure on the early termination charges themselves
- Emergency intervention
  - Policymaker coordinated negotiation with key industry players
  - Agreement reached to cap early termination charges
  - Regulatory process commenced

Balancing market priorities



Coordinator
Policymaker
Confidence builder

Adviser
Profit maker
Confidence builder

Product provider
Profit maker
Confidence builder

Regulatory path

- Confirm the agreement and take it forward
  - Write, consult on and publish the regulations supporting the agreement
  - Signal next steps
- Drive further change
  - Issue updates
  - Address unexpected complexity
  - Keep communication channels open

Regulatory path

- Coordinate diverse initiatives
  - Treating customers fairly – market conduct process
  - Retail distribution review – challenging inappropriate intermediary models
- Demonstrate a willingness to test implementation
  - Technical assessment of compliance

Lessons learned

- Policy development
  - Have the end goal in mind
  - Cooperate with policymaking counterparts in related entities
  - Understand the impacts of changes
  - Aim for balance between rules and principles

Lessons learned

- Relationships with supervised entities
  - Engage actively but keep records of discussions
  - Meet with a wide range of companies and individuals
  - Send strong market signals early
  - Build an effective market conduct capability
  - Foster competitive behaviour on the basis of customer-centricity

Lessons learned

- Customer need
  - Aim to understand the wants and needs of customers
  - Get into the market as much as possible
  - Develop capacity to supervise market conduct

- Risk-based supervision calls for
  - Constant attention to
  - Concerns and potential concerns across the marketplace

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