Investors

INVESTOR FOR RETIREMENT

A Newsletter for Participants of Employee Capital Plans (ECPs) with INVESTORS Funds

Issue 4 / Q3 2021

Drawing by Jerzy Krzętowski

– My son, a pension is not everything – you also have to have money to live on when you grow old!

BY WAY OF INTRODUCTION...

More and more Poles are saving with retirement in mind. The launch of Employee Capital Plans (ECPs) and the related increase in the number of Employee Pension Programs (EPPs) have been an important event facilitating this rise. But many Poles do not treat the topic seriously enough. “I still have a lot of time to start thinking about saving for my retirement” and “I don't earn much and I can't afford to save” are some of the most common arguments presented by people when asked about whether they are setting aside capital to tap into at the end of their professional careers.

Meanwhile, virtually all available forecasts show that our public pensions will be lower and lower in the future. This can be especially painful news for those who have just started working and for whom retirement is a topic that seems not worth pondering over. In our regular series “Everything you always wanted to know about investing”, we explain why we believe it is worth saving for the future.

ON THE MARKETS

- The first half of 2021 was favourable for investors on equity markets, with the indices of all major stock exchanges seeing gains. This came on the back of a recovering global economy, which already managed to recoup a significant part of the pandemic losses. The volume of trade is now higher than before the pandemic, as is global industrial production.
- For both the US and Europe the real test of the uptrend and of investors’ resilience to potential problems may come in this autumn, if – despite an extensive vaccination program – the next wave of COVID-19 is great enough as to force authorities to reimpose economic and social restrictions.
- While this should not change the major trend, given that the previous waves of the pandemic failed to do so, it could provoke some anxiety among investors who, since last November, have clung to the belief that vaccines would make lockdown policies never necessary again.
- In the first six months of this year the Warsaw Stock Exchange did not lag behind the European and American markets, as evidenced by an approx. 15% increase in the main index. The Polish currency also rallied, indicating increased interest of foreign investors in the Polish market.
- The Polish stock exchange is well set to continue its strong run in the second half of the year, although it is not likely that we can expect rates of return as high as in the first six months. For that to happen, the bull market on Wall Street and in Europe would have to continue.
- The good situation on the financial markets is reflected in the results of the “defined-date” funds managed by Investors TFI. The table shows results for the last 6 and 12 months.
- **When evaluating previous investment results of “defined date” funds, it is worth remembering that Employee Capital Plans (ECPs) are a long-term investment vehicle allowing participants to accumulate capital to tap into at the end of their professional careers and beyond. Therefore, the results achieved after several years of operation will be more meaningful for the assessment of the funds' track record.**
- **Returns on Investors TFI’s defined-date funds at the end of Q2 2021 for 6 and 12 months**

Funds	6m	12m
Investor PPK 2025	2.25%	7.99%
Investor PPK 2030	5.24%	14.37%
Investor PPK 2035	8.42%	20.48%
Investor PPK 2040	8.72%	21.55%
Investor PPK 2045	10.05%	24.02%
Investor PPK 2050	10.16%	24.38%
Investor PPK 2055	10.20%	24.23%
Investor PPK 2060	10.05%	24.08%

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> You can be young without money, but you can't be old without it.
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> **– Tennessee Williams,** Pulitzer Prize-winning American playwright, novelist and poet.

EVERYTHING YOU ALWAYS WANTED TO KNOW ABOUT INVESTING

Why save for retirement?

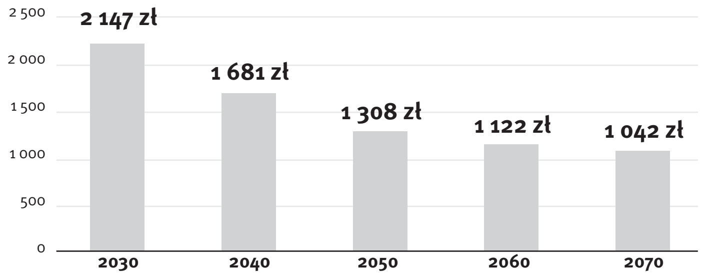
“Everyone should think about their retirement, including young people. One’s future pension should come not only from the public system, but also from other sources like employee programs and individual savings” – says Professor Gertruda Uścińska, head of the Social Insurance Institution (ZUS). Why is it so important to accumulate capital to tap into at the end of one’s professional career? Retirement pensions from the public system are declining in value and will continue to do so. According to forecasts, in 2070 they may – in extreme cases – amount to just the equivalent of today’s PLN 600.

Why so little? The reason lies in the way the public pension system is designed. To put it simply, it assumes that those currently employed pay for the pensions of their parents or grandparents. Although each of us has an individual ZUS sub-account where we accumulate contributions, in reality the amount amassed there is just an accounting entry. The money we pay in is actually spent on an ongoing basis on payouts to current pensioners. What is more, the system is already short of money. Every year, the Social Insurance Fund has to be subsidized from the state budget, i.e. from the taxes we pay. The amount listed in our ZUS sub-account, therefore, is really just a promise that in the future society will pay out a retirement pension in the declared amount.

However, it will become increasingly difficult to deliver on that promise. This is because the ratio of retirees to workers is growing. At present, there are forty retired people for every hundred workers. In 15 years, this number will already reach fifty, and in 30 years – seventy-five. In other words, today more than two workers contribute to financing one pension. If the current trend continues, with time we will be approaching the point where one working person will fund the payout of one pension.

This is of course a bit of a simplification, but it reflects well what lies ahead. The number of working people per retiree affects how big the average pension will be compared to the average salary (this ratio is called the replacement rate). Today, the replacement rate is about 50%, which means that the average pensioner has half the amount available each month to support themselves that the average employee has. However, due to a rapidly aging population, the number of working people is plummeting, while the number of elderly people is on the rise. This will lead to a replacement rate of 32% in 2045 and 23.5% in 2070, according to estimates by ZUS.

Projected Average Gross Pension



Average gross pension in constant 2021 prices, assuming earnings at the level of national average salary. Source: original calculations based on ZUS data provided in response to Adam Szłapek's parliamentary inquiry of 7 June 2021. Calculations in accordance with ZUS methodology, adjusted for the tax-free amount.

In other words, in 50 years, the average pension will be less than a quarter of today's average salary – that is, about PLN 1,096 (gross). In the case of the minimum salary, the amount is less than PLN 600.

What should I do if I can't afford to save?

Imagine having to live on less than half of today's paycheck. Tough to get by, right? And that's the "as of today" perspective. Every year, the prospect of living on a public system pension will become harder and harder to imagine. That's why saving for retirement is really a necessity, not a choice. The earlier you start saving, the more money you will accumulate.

Participation in an Employee Capital Plan (ECP) is certainly a good starting point. All the more so because the design of ECPs assumes that the employer finances part of our savings. However, it is worth considering going even further. The structure of ECPs allows participants to declare an additional contribution of up to 2% of their salary. The declared amount can be changed at any time. It is also possible to opt out of additional payments at any time. ECPs are one of the most cost-effective saving methods (cheapest for the participant). Taking into consideration the prospect of decreasing pensions from the public system, it is worth considering how to take advantage of the opportunities offered by Employee Capital Plans.

The Polish pension system also offers other attractive options for saving for retirement – Individual Retirement Accounts (known by the Polish abbreviation IKE) and Individual Retirement Security Accounts (known by the Polish abbreviation IKZE). We will write more about these solutions in the upcoming issues of *Investor Emerytalny*.

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NEWS FROM THE WORLD OF PENSIONS

What's next for Open Pension Fund reform?

The bill winding up the former Open Pension Fund system was meant to enter into force (with some exceptions) on 1 June 2021. The bill provided for the transfer of funds accumulated in the Open Pension Funds to newly created Individual Retirement Accounts (to distinguish them from the 'old' IKE, they are often referred to as IKE+) or to individual accounts in the Social Insurance Institution (ZUS). The default solution was to transfer the funds to IKE+, which would incur a conversion fee of 15% of the accumulated capital. With this fee, we gained the private ownership of the funds, meaning that they would be inherited in full. The transfer of funds to ZUS, on the other hand, would not entail any costs, but in the case of death the accumulated savings would be lost. In addition, in order for the funds to be transferred to our account in ZUS, we should fill out and file the necessary documents.

Despite the fact that the reform was supposed to enter into force on 1 June this year, we still do not know what form the potential liquidation of OFEs will take, and the bill itself has been shelved. Why so?

The reason is the increase in the standardized personal income tax deduction (the “tax-free amount”) to PLN 30,000, including for pensioners, as planned in the announced ‘Polish Deal’ stimulus program. This provision undermines the previous argumentation for charging a 15% tax for transferring funds to IKE+. The conversion fee was to be roughly equivalent to the tax payable on pension payments from ZUS. If the personal income tax allowance is increased, this argument becomes unjustified. Thus, it seems it will be difficult to proceed with the OFE liquidation reform in its current form. The tax bills related to the Polish Deal may be ready by the end of summer, so perhaps they will shed some light on the future of the nearly PLN 150 bn that remains accumulated in OFEs. We will keep you informed about any progress on this issue in subsequent newsletters.

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