MINET THOUGHT LEADERSHIP

IMPACT OF COVID-19 ON VOLUNTARY PENSION SCHEMES AND INVESTMENT VEHICLES

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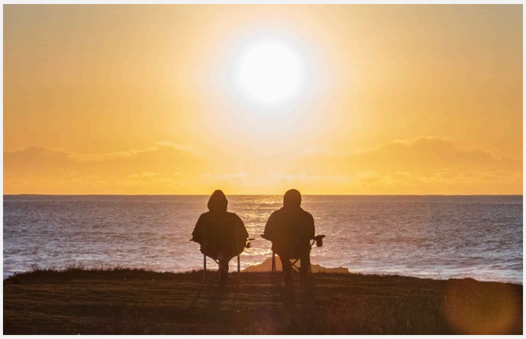

The COVID-19 pandemic has raised serious concerns for everyone about retirement security, and even more so for those who are due for retirement. The pandemic has seen many workers being laid off by their employers, causing a rise in global unemployment rates (8.3% from 6.7% in 2019). Coile & Levine furthermore claim that these increased levels of unemployment also threaten economic well-being of those nearing retirement. Some employers, due to stress on their financial statements, have resorted to reducing employees' salaries instead of laying off employees, which in turn impacts people's standards of living and choice of investment vehicles.

Covid-19 has, to a large extent, affected those employees, who are about to retire vis-à-vis retirement savings. Retirement benefit schemes of employees, who contribute voluntarily have been affected the most. Events that affect the source of joy to investors (return on investments) have had and will have long lasting effects on future benefits. During the pandemic, we've witnessed panic buying of food and other items. Due to that action, prices of various goods and services scaled up dramatically. On the other hand, due to lockdowns in various areas, fewer quantities of products were exported by local markets, thus increasing domestic supply and circulation of goods, leading to a reduction in prices. Supply outweighed effective demand in many sectoral markets. A case in point is the price of matooke in Uganda, which declined from an average of UGX 25,000 to an average of UGX. 5,000 per bunch.

In Uganda, pension schemes run by voluntary contributors create special Boards of Trustees that oversee the schemes' performance, including investment. Trustees, through their fund managers, diversify into traditional and non-traditional investment assets and vehicles. However, most retirement contributions are invested in shares within the financial markets. The value of one's retirement savings or contribution is therefore linked to what happens in the financial markets. In the case of shares, when their values or prices are increasing, one's savings will also be growing and the opposite when share prices fall. There is a notable trend that share prices have fallen in most countries in the world, including Uganda, due to the impact of COVID-19. South Africa, for instance, reported a 51 percent economy contraction in the second quarter of 2020 due to the pandemic. The point is that the pandemic has caused impulsive reactions and change in consumer behavior, all to the detriment of the retirement, personal financial planning and savings culture. Fragmentation of global trade as well as demand and supply linkages have led to price volatility and tumbling of financial markets.

But all is not lost. Long term investors have seized this opportunity by cherry-picking undervalued stocks, with an aim of making better returns in the long run which in turn impact retirees' retirement savings. Reports indicate that expected rates of return to both equities and bonds have declined in recent years. If this development goes on unbated in the investment space, it will cease being a risk, but will have a clear implication for investors saving for retirement. Older workers, who are nearing retirement, will run the risk of diminished economic well-being due to the shock that reduces their savings, pension, or social security benefits.

Some schools of thought advance that older workers retire earlier in response to an economic downturn. This pattern is evident today due to the premature disinvestment of assets in the bid to settle the overwhelming numbers of claims for retirement benefits. This is predominant in voluntary schemes, where the scheme or fund rules allow members to access their benefit at leaving their employers. The benefits withdrawn are taken to help these workers to settle their short-term liabilities due to the abrupt shock of losing their jobs or reduced daily income, thus inducing the risk of many years of diminished financial wellbeing.

A review of data on previous, similar pandemics (e.g. the Spanish flu), gives us a potential snapshot of the economic impact posed by the current pandemic of COVID-19. Mirroring on the aforesaid, Fernandes asserted eloquently; ". . . the world today is facing a different pandemic, evidenced by zero correlation between economic impact and mortality rates but rather the reaction of governments, companies, consumers and media all creating a simultaneous demand and supply shock, which is causing various economies to contract." The shrinking economies have caused a decline in return on investment, which further suggests a shrink in retirees' accounts.

Some economic commentators suggest that individuals should respond to negative stock market shocks by reducing their consumption of normal goods (including leisure) and delaying retirement. However, this hasn't been the case in Uganda and other countries in the region as many people without social protection programs have resorted to claiming for their retirement benefits across the various platforms to help them cushion short term shocks rippled from the COVID-19 pandemic.

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References:

- *Coile and Levine - https://www.aeaweb.org/articles?id=10.1257/aer.101.3.23*