SESSION 2 – DEBT MANAGEMENT

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(The answers which are given are general in nature, and therefore do not constitute financial or other professional advice. The answers do not take into account your specific circumstances and should not be acted on without full understanding of your current situation and future goals and objectives by a qualified financial adviser.)

Q. How does Old Mutual Budget Repair Service differ from debt review?

The Budget Repair Service aims to help you to take control of your finances and plan to get out of debt or reduce debt prior to retirement in a structured way. With Budget Repair you understand your current spending profile, which can be used to amend your spending to create released affordability to repay debt faster. This not the Debt Review Service in terms of the National Credit Act.

Q. With the huge drop in income post-retirement, does the 35:25:35 spending rule still apply?

In many cases, post-retirement income drops but some of your expenses will also reduce. The golden rule is that you need about 70% of your last year's income to maintain your lifestyle. This in some cases may include some debt repayment. The first important issue is to have a place to stay and to make provision for medical aid and short-term insurance. Medical aid cost will increase over time and short-term cover may reduce over time. The amount left is used to pay normal living expenses. If this amount is sufficient to cover your living expenses you may well be able to maintain your living standard. If the answer is that it does not cover your living expenses this will require a planned reduction in lifestyle. It is for this reason that it is recommended that debt be repaid prior to your retirement.

Q. Is debt consolidation a good way to pay off debts?

Any new loan attracts interest, initiation fees and new monthly service fees. A consolidation loan is only beneficial if the total cost of the new loan is less than the sum of your current costs and interest, and you do not extend the repayment period. If you extend the repayment period this may well increase the total cost over the period. This means from a cost point of view the consolidation loan may increase the cost which is not recommended.

It may be more cost effective to use your free cash flow to repay debt faster. Start with the lowest debt and increase your payment and when it is completely repaid, close the account and repeat the process.

Some Consumers use their home loan to consolidate debt. This may reduce your cost but do not extend the payment over the full term of your bond. If your loan repayment was, for instance, R2 500 it will be beneficial to settle the debt from your home loan but also increase your bond repayment by R2 500. This will repay the debt over a shorter period and result in a cost saving.

Q. How do you decide which debt to get rid of first?

In order to get into the discipline of repaying debt it is recommended that the smallest debt be repaid first. The pleasure of repaying this debt and closing the account will be the inspiration needed to repeat the process.

Q. What are the typical or examples of financial debts that a pensioner should avoid?

Any debt that a pensioner cannot afford is bad debt. In some cases, a pensioner might have a home loan and can repay the debt. The preferred option is to be debt free when on pension. This also decreases stress.

Q. Am I supposed to ask my employer to increase my contributions to my retirement fund or go straight to Old Mutual?

You need to discuss and arrange this with your employer. Once agreed, your employer will ensure that the increased monthly contribution is paid over to Old Mutual on their monthly payroll.

Q. I took a home loan for R1 500 000 and I am 61 years old. How will this affect my retirement?

If you can afford the repayments, the effect will be minimal. If you can, accelerate the repayment of the home loan. If it is difficult to pay the home loan while in retirement, consider scaling down to ensure an acceptable pension budget.

Q. Would it be advisable to defer retirement by another two years? Reason is impact of COVID -19 on retirement savings. Would employers consider this?

The longer one can work and earn a salary the more one should be able to invest for their future retirement. As to whether one's employer will consider this deferment (i.e. continue working for that employer) is entirely up to you and your employer to discuss and agree upon. Any decision is to be taken with extreme care and all things need to be considered. It is therefore, recommended that you chat to your financial adviser who can give you holistic advice on your personal needs.

Q. I am in a fortunate position in that I am debt free, yet I am still extremely concerned whether I would be able to survive on my pension. Is this normal?

It is normal to be concerned but being free already reduces stress. To reduce uncertainty, we recommend you do a retirement budget as explained in the presentation.

Q. Is the trend that pensioners' debt is rising and they therefore tend to be more reliant on family support?

Debt exposure overall has increased but it is good practice to implement a debt reduction before you retire so you can be debt free prior to retirement. If this is not possible, consider working a bit longer to continue a debt reduction plan.

Q. If I have a house for rent, is it better to pay it off? What is the tax implication?

You will be required to pay tax on the rental income. If you can afford to, it is better to repay the bond faster and have an asset on your balance sheet.

Q. What percentage increase should one budget for medical expenses in retirement?

The percentage will depend on the medical aid plan used. The cost prior to retirement can vary from 5% to 20% of after-tax income. You can calculate your medical aid to after tax income ratio by using the current medical aid cost as a percentage of your after-tax income and if you continue with the same medical aid cover, calculate medical aid cost as a percentage of your after-tax pension income. It is also important to note that it is expected that medical costs will continue to increase well above the inflation rate.

Q. I am contributing extra funds into my pension monthly, should I be rather using those funds to reduce my debt?

It is good practice to save more for your pension. If possible, maintain this practice and consider a debt reduction plan.

Q. How does Octogen make money from the Budget Repair process?

Normally the Employer pays the consultation fee.

Q. Can your company help with reducing debt and negotiating better rates without having to file for insolvency or debt review? If so, what does the service cost?

Credit Providers are normally not amenable to amend interest rates on current credit agreements. The best place to negotiate the best rate is on application.

Q. I am retiring within six months and I have a Home Loan, Credit Card debt and a Personal Loan. What should I do to manage or reduce all of this debt?

It all depends on your current cash flow but if possible, it is recommended that you increase payment and repay all debt excluding your Home Loan. Best practice is to be debt free when you go on retirement.

If this is not possible and you have funds available in your retirement income then continue to repay debt until repaid in full. If possible, repay faster until you are debt free.

If you have a Home Loan and you can afford the Home Loan repayment based on your retirement income continue with repayment. It is also recommended that you increase payment to reduce repayment term and reach debt free status in retirement.

If you cannot afford the Home Loan repayment consider selling the property and use the surplus to downscale living arrangement.

Q. Can you share a good budgeting or expense tracking tool that will help me with repayment of debt?

The golden rule is to start to reduce controllable expenses. This would include food, clothing, water and lights, cellphone expenses, entertainment, etc. Identify where you can spend less and use that money to repay debt.

The next category includes some tough choices: Cancel or suspend DSTV, move to prepaid on your phones, move to less expensive banking option, get comparative quotes on your short-term insurance, sell you vehicle and buy less expensive but good 2nd hand vehicle.

The driver in all the options mentioned above is a personal choice and commitment to make it happen. The first step is the most difficult but success will make next step easier.

Q. If you are under debt review, is there any way to settle your debt when you retire without having to use your pension?

You will need cash to settle debt and where this is not possible you can consider once in a lifetime lump sum Retirement lump sum withdrawal which is zero rated for tax purpose. The current maximum is R500 000.

Q. I have investments and debt. Should I take money out of my investments to pay my Credit Card in full, or rather leave the investment and carry on paying off my Credit Card monthly?

The nature of the investment will need to be reviewed in making a choice. Let's use two examples:

- If you have fixed deposit with return of 4% and Credit Card Debt at interest rate of 26% you will save money to repay the debt in full.
- If you have a Retirement Annuity it is possibly better to continue to stay invested and not cash in the policy to repay debt. There could be a cost of cashing in your investment.

Q. I have two Home Loans. One is bigger than the other, but the smaller one has higher interest. Which one should I focus on paying off first?

Two options can be considered:

- Increase repayment on the highest interest rate Home Loan and repay the debt and cancel bond to prevent further use of the bond to access debt. You will also save monthly fees.

- If you are close to retirement it may a be better to increase repayment of bigger bond with the aim to repay or substantially reduce balance prior to retirement.

Q. I'm currently under debt review, but I want to get out of it. I have paid most of my debts except my bond, but there are arrears amounts still owing. Do I have to settle all the arrears before I can leave debt review?

To get out of Debt Review all debt, excluding Home Loan, must be repaid in full. Recommend that you ask you Debt Counsellor for outstanding balances and plan to repay as fast as possible.

Q. How long does it take for your credit record to be cleared after you finish debt review?

Once a Debt Counsellor has issued a Clearance certificate the Credit Bureau has to be updated in 7 working days. It is however important to note that internal information might still be retained by Credit Provider systems. Once you receive a Clearance certificate and you need new debt approach a Credit Provider where you did not have any debt. Some Credit Providers such as OMF may well offer debt when Clearance Certificate has been obtained.

Q. What is the difference between Debt Review and Debt Counselling?

No difference whatsoever. The National Credit Act uses both names but same rules apply.

Q. The 70% rule you refer to is decades old. Longevity risk has increased substantially, so this may stave off poverty, but it won't allow for a quality lifestyle. Please comment.

Yes, but it is based on the reality that once you are in retirement some of your cost will fall away. This may well include items such as travel cost, retirement saving, less expensive insurance, lower phone bill, etc.

On the other hand, you are correct that longevity is increasing and added to this is cost increases experienced in medical provision as well as and increase pricing.

The reason for mentioning the 70% rule was to point out that in most cases some cost will disappear at the point of retirement but you need to plan for increased cost of living to cater for longevity and cost pressures.

Q. Will the staff interest rate I receive on my Home Loan and vehicle finance change when I retire from Old Mutual?

Please contact your HR Department to confirm the rules applicable.

Q. Have average household expenses increased in 2020 due to people working from home as a result of Covid-19?

No, the opposite has happened. Consumers have cut back on many household expenses such as food, clothing, entertainment and travel. Many consumers have used this experience to cut back on a more permanent basis.

Q. **If your partner is in debt due to the number of Credit Cards they have been issued, is there a way to get banks to lower the credit amounts they are offering over time to help the person lessen their debt?**

Banks can be asked to change the limit to a reducing only limit. This will mean no new debt will be allowed and debt is repaid. This option is a good option for consumers to follow and all you need to do is to write to the bank with an instruction to change the limit to reducing only limit and agree on repayment term for the balance. In terms of the National Credit Act Consumers have the right to do ask for debt to be placed on a reducing basis.

Q. **What percentage of my after-tax income is normal or acceptable to be used to pay rent?**

This is a personal choice but a good rule to use is to ensure that rent and debt repayment combined do not exceed 35% of your after-tax income. When this is the case you should be able to save for retirement and cover risk and pay normal household expenses.

Q. **What percentage of my net salary should I be putting towards an emergency fund?**

A good rule is to use 5% of you after tax income with the aim to have a minimum of 3 months after tax savings in a separate savings account.

Q. **With the government wanting to tap into our retirement funds, why can we not use the value of our funds ourselves to pay off our debts, etc.?**

It is normally not advisable to use retirement savings to repay debt simply because this will put you with impossible task to save enough for your retirement. History has shown that people who use pension saving to repay debt normally do not have sufficient funds to retire.

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