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The central concept underlying the LRIS is that suitable, low-cost and prudent institutional-type life cycle funds, which are "pooled or "commingled" in some form, could be offered to CPF members based on their age and risk tolerance. The pooling of investment choices enables lower expense ratios to be "negotiated" by the plan's sponsor. FILE PHOTO

Where are we on the CPF Lifetime Retirement Investment Scheme?

This scheme is meant to grow everyone's savings in a prudent and low-fee manner. **By Joseph Cherian and Emma Yan**

IT HAS been exactly three years since the CPF Advisory Panel recommended to the government the need to study the provision of the Lifetime Retirement Investment Scheme (LRIS), a prudent, low-fee option for those who prefer a professionally guided manner to invest and grow their "surplus" CPF retirement savings.

Specifically, members with over $20,000 in savings in their Ordinary Accounts (OA) and S$40,000 in their Special Accounts (SA) can tap the LRIS option if and when it comes online.

The CPF website reports that there are 3.9 million CPF members with a combined S$137.6 billion in the OA and S$102.9 billion in the SA as of March 2019. Only about S$22.5 billion is invested under the CPFIS (in both CPFIS-OA and CPFIS-SA). There is therefore a vast amount of investible CPF funds that presumably could still be deployed in growth assets, that is, for CPF members wishing to invest their (surplus) retirement savings.

What is the LRIS?

The proposed LRIS is a slow and steady way of potentially growing one's long-term retirement savings in the manner of private investment paradigm. We should insert a caveat here that the current tiered savings rate provided within the CPF Board's Special, MediSave and Retirement Account (or SMRA) and OA accounts, for example, is up to 6 per cent per annum for the first S$30,000 in savings in the RA for those 55 years old and above for SMRA, and not lower than the legislated 2.5 per cent per annum minimum for OA, are hard to beat.

However, members have expressed their desire to potentially earn even higher returns from their CPF savings by taking some investment risk. But they feel they lack the financial acumen, time or resources to actively manage their retirement savings and accounts. In such circumstances, simple-to-understand, low-cost, well-diversified and potentially customised institutional-level retirement products to meet such members' needs would be desirable.

Unfortunately, the CPFIS programme in its current form is a colossal, and perhaps confusing, retail fund scheme, where retail-type investment products are marketed and sold to individual investors. Retail-type investment products typically impose much higher fees. This is where the LRIS could add great value.

A side note on the US' 401 (k) plan would be instructive here. This plan is an employer-led, tax-deferred, institutional-level retirement programme for eligible employees. The plan sponsor (usually the employer and/or its representatives) chooses the investment products to offer on its platform, as well as negotiating the institutional-level fees associated with such products.

Academic- and industry-led studies reveal that the all-in, institutional-level fees on certain well-managed 401 (k) plans' investment products, or total expense ratios, can end up being negotiated to as low as 0.5 per cent, with no sales loads, charges or commissions to boot.

Additionally, many 401 (k) programmes offer a default investment option, which tend to be life-cycle products – these are simple-to-understand, low-cost, well-diversified products with a risk-adjusted "automatic glidepath" that calibrates target risk levels from the start of a cohort's savings and accumulation period (for example, more in risky growth assets when one is younger) to retirement (for example, a greater proportion of the investment corpus in safe fixed-income assets as one approaches retirement and prepares for decumulation).

The good news in this direction is that, firstly, the Singapore government announced in March 2018 that the sales charge for the CPFIS programme would be lowered. The first step in the process entailed reducing the sales charge from 3 to 1.5 per cent from Oct 1, 2018.

The second step will be to remove loads by Oct 1, 2020. The long runway to zero is to give local financial advisers more time to adjust to the revised CPFIS fee structure, which is being lowered across the board.

Secondly, we need simpler, low-cost, well-diversified and potentially customised institutional-level retirement products for CPF members, such as life cycle funds. This is particularly true for younger people, who have a longer runway to retirement and wish to invest their retirement savings for higher potential returns because of larger balances and greater expectations in terms of their lifestyle in retirement.

The LRIS proposed by the CPF Advisory Panel in the latter half of 2016 – which the government accepted and continues to work on implementing – was designed to meet this need. The central concept underlying it is that suitable, low-cost and prudent institutional-type life cycle funds, which are "pooled or "commingled" in some form or the other, could be offered for the various CPF member cohorts based on their age, risk tolerance and other circumstances.

It is because there is this pooling of investment choices, primarily to achieve scale in assets under management, that lower expense ratios could be "negotiated" by the plan's "sponsor", whoever that may be.

The exact types of life cycle products and the associated financial engineering that may be required are a matter of investment science. That is best left to the experts, such as independent financial investment advisors, financial institutions and select finance academics.

It is important to note that in order to get the LRIS strategy operational, seed capital is required to incubate these life cycle strategies. The seed capital will keep fees as low as possible at the outset, given that economies of scale in assets yields lower fund fees and thus total expense ratios. As members opt into the LRIS programme and the appropriate scale in assets under management is independently attained, the seed capital could be judiciously withdrawn.

More customisation possibilities

One innovation not discussed is the customisation and automation of such plans. Financial technology and associated digital asset management and advising services are rapidly evolving to a level where the LRIS – or similar products within the CPFIS – would meet the simple-to-understand, low-cost and well-diversified test. Smart, well-trained financial robo-advising – that is, learning systems such as neural networks, artificial (and human financial) intelligence and deep learning, along with the availability of training data sets (such as big data) for this learning – can also be used to further customise members' individual retirement portfolios and life cycle glidepaths to meet their personal lifestyle requirements.

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Finally, and in the ultimate stage to the long march to a worry-free retirement, we envision blockchain technology someday democratising members' access to the best and highest-quality alternative investment opportunities. Appropriate vehicles offered by hedge funds, private equity or venture capital could be utilised in order that properly qualified and assessed members may improve their retirement savings' risk-adjusted expected returns even further. The additional hope is that financial technology and investment science would help lower the denominations and the investment costs involved in alternative investments, both of which are currently extremely high.

The CPF Advisory Panel's report on the LRIS is available at https://services.mom.gov.sg/cpfpanel/

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