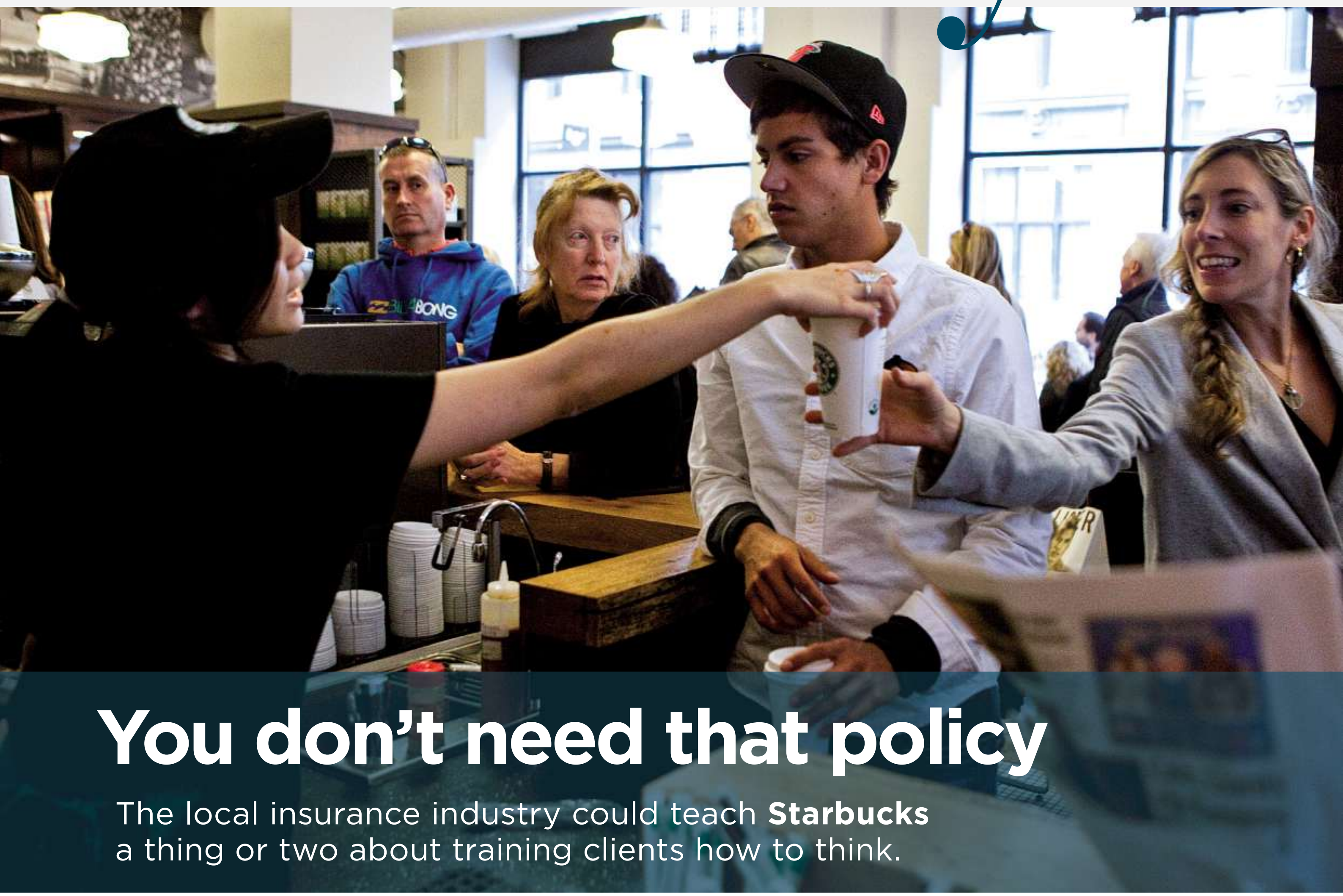
Money



You don't need that policy

The local insurance industry could teach Starbucks a thing or two about training clients how to think.

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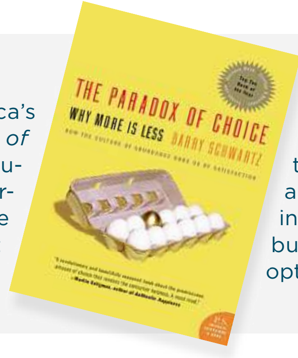
Anne Morriss, co-author of *Uncommon service: How to win by putting customers at the core of your business*, has been getting a lot of publicity recently. She believes that one of the reasons behind the continued success of Starbucks is that it has managed to "train" its customers. Her theory is that Starbucks created its own language as a means of getting orders through more efficiently, thereby moving the queues a lot faster. In the past a customer may have ordered a "large cappuccino with an extra shot of espresso to take away" – or "a big cappuccino, double espresso in a take-away cup". Customers were essentially using different words to say the same thing. Nowadays such a customer using the Starbucks language is likely to say something like "double tall cap with wings".

Starbucks staff were supposedly trained shout out customers' orders in this new language, thereby "motivating" the customer to use this "language" in future. They even have lovely looking brochures that customers can take home to learn this language, says Morriss. This Pavlovian like manipulation seems to have contributed quite significantly to faster moving lines and therefore happier clients. That is the theory at least.

My experience with clients and potential clients over the past year or so leads me to believe that the local insurance industry could teach Starbucks and Mor-

TOO MUCH CHOICE

Are too many options paralysing South Africa's retirement savers? In his book *The Paradox of Choice: Why More Is Less*, Barry Schwartz documents research that shows that employee participation in pension plans lessened as the number of choices between investment options increased. For every extra investment option, there was a 2% drop in people willing to invest in the pension plan. Judging from its latest proposals to reform the retirement industry, Government is clearly moving towards standardisation in the more than 2 700 pension funds in SA. This may mean consolidation in the funds, but also that investors only have one investment option – which won't require financial advice.



riss a thing or two about training customers how to think, or what language to use when it comes to investment products.

I had a call quite recently from a wealthy client who I have known for many years. After the small talk and exchange of pleasantries, the conversation went something like this:

Client: "The reason for my call is that I want to set aside money for the kids' education. Do you sell education policies?"

Me: "No! But why do you want an education policy?"

Client: "It's for their education!"

Me: "So?"

Client: "You're confusing me!"

This conversation echoed one I'd had a few weeks before with another client. His comment was: "I'm fine on the retirement side – I have a retirement policy. What I want you to help me with is an investment policy."

It seems that for many people, the solution to their financial objectives is some sort of policy. I need to save for education – give me an education policy! I want to save for retirement – give me a retirement policy! I want to start an investment to build wealth – can I have an investment policy?

While the habit of investing has to be encouraged, it appears that many invest-ors have been trained to think in a certain way about how to go about it. Unfortunately for many, this is unlikely to help them achieve their investment goals. It is wonderfully efficient for the companies that do sell these products, as they are able to get the client to sign up quite quickly, and provide them with some peace of mind about having done the right thing, or at least it seems to be the right thing.

POLICIES ARE NOT FOR EVERYONE

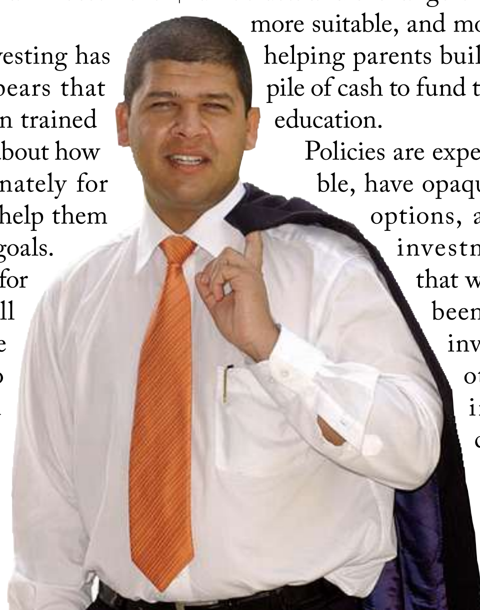
For investors with total annual income of less than R250 000 a year there is no real benefit to be had by investing in an endowment- type investment. There is no tax advantage for them, and they will be giving up liquidity and flexibility, and gaining nothing in return for doing that.

The only benefit that could come from having funds in an endowment is that they would not form part of the investors' estate and therefore not attract executor's fees (a saving of 3.99% max).

When it comes to investment objectives such as education, retirement and wealth building, a policy should not be the answer for most South Africans. I have yet to hear of a school that asks a parent for their education policy. School fees are payable in cash, and the school is certainly not interested whether the cash is proceeds from a policy, or a loan, or a donation to the parent – they just want the cash.

Cheaper investment options such as unit trusts and exchange-traded funds are more suitable, and more efficient at helping parents build up a decent pile of cash to fund their children's education.

Policies are expensive, inflexible, have opaque investment options, and often tax investment returns that would not have been taxed in the investors' hands otherwise. An investor that contributes R500 a month to a unit trust is likely to be better off than one that contributes to an equivalent fund in a policy. It is only once investors have used up their tax exemptions that they should consider a policy.



Craig Gradidge

When it comes to retirement policies such as retirement annuities, I tend to agree that they are an efficient means of saving for retirement. They offer meaningful tax benefits and the assets are protected.

However, the average investor would be wise to ensure that they are investing in cheaper, new-generation products which offer them flexibility, choice and transparent pricing. These products are better designed to meet the interests of investors than any other party (product provider, adviser, asset manager, etc).

Old-generation products often pay huge commissions upfront and have onerous penalties that kick in when clients need to amend the initial contract in any way. New-generation retirement annuities pay for advice and other admin fees as and when premiums are paid, resulting in more of the investors' funds actually being invested.

It is important that investors understand the implications of simply using the language of the industry and buying the product that "addresses their particular need". This sort of efficiency in thinking is likely to benefit the product providers, their shareholders and their salespeople more than the investor.

Only by following a robust investment planning process, and interrogating the solutions offered, will investors be able to achieve their investment goals and objectives. ■

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