Business and Finance

Looking at retirement in the next century

Until recently, Canadians have more or less taken for granted that a combination of government programs and employer pension plans would guarantee their retirement income.

But now planning for retirement has become more complicated because of a number of new, unknown variables

Government Programs

The Canadian Pension Plan will survive. The federal government and the provinces are currently locked in debate over the future of the CPP. But it's clear there is political will on all sides to retain the CPP.

There may be changes such as raising the retirement age, reducing some benefits and an increase in premiums.

We expect premiums will eventually level off at around 10 per cent of earnings (the 1996 figure was 5.6 per cent divided equally between employer and employee).

Whatever changes are made to the plan, it is clear that CPP payments will not be adequate to support the average person in retirement. CPP payments should be regarded only as an income supplement.

One piece of good news is that the government is unlikely to impose a special tax on these payments.

Universal programs will disappear

The proposed Seniors Benefit represents a major shift. It moves us from a universal old-age support program to one tied more directly to need. The message is clear: Higher-income, older Canadians cannot expect any government support in future, either directly or in the form of tax concessions.

Private pension plans

Because of the high cost of defined-benefit programs, employers are looking at other options.

Most of the new plans are either group Registered Retirement Savings Plans or defined contribution money purchase pension plans, with no income guarantees.

The effect is to shift responsibility for retirement planning and investment decision-making onto the employee. Employees will have to decide where their retirement savings should go and ensure that the eventual income will be adequate for their needs.

The climate has changed. The minimal inflation and low, stable interest rates we know today should continue into the early part of the 21st century.

These patterns are not just a Canadian trend – it's a worldwide pattern, as governments and central banks learn how to manage economies more efficiently.

For retirement planning, it means returns on RRSPs and pension plans will be lower in the next decade than they were in the '70s and '80s.

The unknown factor

As the federal and provincial governments eliminate their deficits and start reducing their total debt burden, their spending power will increase. Governments may use some of the money saved on debt servicing to reduce taxes. Or they may opt to build political capital by improving health care and education or sweetening the benefits offered to retired Canadians.

If tax reduction is the choice, you'd be well-advised to use some of the extra money to add to your retirement savings program.

Ultimately, the most effective way to deal with the retirement uncertainty that lies ahead is to increase your personal savings.

This article was submitted by John McCallum from Royal Trust.

Top Priority

Generation X: Take advantage of low rates by using savings on mortgage payments to add to retirement savings program.

Baby Boomer: Take a hard look at anticipated retirement income from all sources. If need be, accelerate savings.

Soon to be retired: Structure your retirement income plan to ensure required cash flow.

Retired: Improve after-tax returns, for example, when interest rates are low, dividends are often more effective investment choices.

Future Strategy:

Generation X: If tax cuts materialize, save some of the money and join a pension plan or group RRSP.

Baby Boomer: Invest prudently. Retirement isn't far off; you can't afford a major loss but need growth for longer life expectancy and more active lifestyle.

Soon to be retired: The mandatory age for winding up an RRSP drops to 69 in 1997. If you're effected, start planning now.

Retired: Watch changes to government support programs, including tax breaks. If you're effected tell your federal and provincial legislators.

Outlook:

Generation X: May carry a disproportionate share of the cost of supporting retired people.

Baby Boomer: Likely to be hardest hit by government cutbacks. Possible offset – tax cuts while still in your earning years.

Soon to be retired: Well positioned. More likely to have well-funded pension plans. Low inflation will be a big bonus.

Retired: Better off will lose some government benefits, but effect should be minimal. Low inflation will mean stable purchasing power.