# Qualitative Analysis of Early Pension Withdrawal in Defined Benefit Schemes: A Case National Pension Scheme Authority (NAPSA)

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## ABSTRACT

This paper aims to look at model retirement behavior with a focus on early retirement where there is an option for "buy-outs". An employer can offer employees generous pension programs if the employees agree on early retirement. Earlier studies have neglected such offers, but in doing so, estimates of the individuals' responses to financial incentives in a retirement decision are likely to be biased upward. Design/methodology/approach The authors propose an estimation strategy where the retirement decision and the accesses to early retirement pension (ERP) offers are estimated in a simultaneous equation system, yielding unbiased estimates of the model parameters. They apply the model using detailed Swedish register data.

### Findings

The results indicate that the marginal effects in retirement probability with respect to a change in financial incentives is less pronounced if ERPs are accounted for. Further, results imply that the early retirement probabilities would decrease, depending on year, by 14-28 percent for males and 7-18 percent for females if ERP offers were absent.

### Research limitations/implications

As the motives for early retirement pensions most likely stem from how the collective agreement occupational pensions are financed, this emphasizes the need for a debate on the preferable construction of these systems. This becomes particularly important in view of the increased old age dependency ratios that are expected in the near future.

### Originality/value

Although these offers have important policy implications they have received limited attention. This paper fills an important gap in the existing pension literature, and it analyzes early retirement and tries to assess the importance of special early retirement pension programs for these outcomes.

**Keywords:** Retirement, Pensions, Older workers, Financial benefits

## INTRODUCTION

Pension systems of modern times can be traced back to the Bismarckian social welfare system which was introduced in Germany in the late 19th century (Hu & Stewart, 2009). Pension systems were created to alleviate poverty among the elderly and vulnerable in society. Pension coverage however remains low as the International Labour Organisation (ILO) estimates that only one in five workers has pension coverage (Stewart & Yermo, 2009). Social protection systems, just like education and health are contributing factors to the development agenda. Some of the positive impacts pensions have had according to (Help Age International (2006b) as quoted by (Stewart & Yermo, 2009) include reducing the poverty gap ratio by 13% and increasing the poor's income by 50% in South Africa, social cash transfers in Zambia have improved school attendance for orphans and pensions in Latin America contributed to rural urban migration reversal, decreased birth mortality rates and provided households with liquidity (Stewart & Yermo, 2009).

In Zambia, several Social Security Schemes exist. First is the National Pension Scheme Authority (NAPSA) which is the main social security scheme and was born of Act no. 40 of 1996 overtaking the Zambia National Provident Fund (ZNPF) which came to an end in January 2000. Second is the Local Authorities Superannuation Fund (LASF) Act chapter 284. Thirdly, the Public Service Pensions Fund (PSPF) Act chapter 260. Fourthly, Workers Compensation Fund Control Board (WCFCB) Act no. 10 of 1999 of the laws of Zambia and fifth is Occupational Pension Schemes; the Pension Scheme Regulation Act, 1996 (Banda, 2017).

NAPSA was established in February 2000 to provide social security to both private and public employees. PSPF was established to provide pension cover to public service employees only. LASF on the other hand was established to provide coverage to local authorities and utility company employees such as the councils, water, and electricity utility companies. Finally, WCFCB was established to provide disability suffered or disease contracted during employment to both public and private sectors apart from the state (Banda, 2017).

As of 2015, the retirement age was amended in Zambia from 50, 55, 60 for early, normal, and late retirement respectively to 55,60, 65 for early, normal, and late retirement respectively. This meant that the access of retirement pension benefits at NAPSA could only be after the age of 55.

## LITERATURE REVIEW

This chapter examines literature pertaining to qualitative risk analysis, Pensions, and risk management in Pension Funds. The literature reviews various journals, books, and articles in this knowledge area to identify the research gap. The approach used in the search of literature was based on the use of keywords such as pension risks, risk analysis, pensions, and early pension withdrawal. The newness of literature and number of citations were the acceptance criteria applied to the select literature for this chapter.

### Risk Management

Risk management is defined in the Project Management Book of Knowledge (PMBOK) as the process of planning, identifying, analysing, response planning, implementation, and monitoring of project risks (Project Management Institute, Inc, 2017). The PMBOK further states that increasing the probability and impact of positive risks while decreasing the probability and impact of negative risks for the purpose of optimising project success are the objectives of project risk management. The process begins with the risk management plan which defines how project risk management activities will be conducted, individual risks are then identified and documented, and a qualitative risk analysis is then performed which is the process of prioritising the identified risks according to the probability of occurrence and impact. A quantitative risk analysis is then conducted which is a numeric analysis of the individual project risks. Risk responses are then planned which is the process of developing options, strategy selection and actions to be taken to address the project risk. The risk responses are then implemented according to the risk response plan. The risk implementation plan is finally monitored by tracking the identified risks, identifying, and analysing any new risks and evaluating the risk process effectiveness throughout the project life cycle (Project

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Management Institute, Inc, 2017).

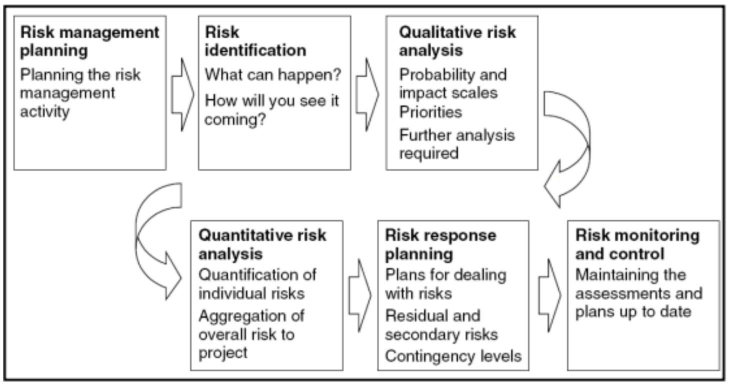


Figure 2 the PMBOK guide project risk management process (Hui & Davalos, 2009)

## Quantitative risk analysis

Quantitative risk analysis is defined by the PMBOK guide as the numerical analysis of project risk effect (Hui & Davalos, 2009). Quantitative risk analysis usually involves complex analytical methods that require computer programs to estimate the probabilities of individual uncertainties.

## Qualitative risk analysis

According to (Project Management Institute, Inc, 2017), qualitative risk analysis is the subjective process of assessing the probability of occurrence and impact of identified project risks on project objectives. The process is subjective because it is based on the project team and stakeholder's opinions. A qualitative risk analysis has two objectives, risk identification and initial risk assessment (Hui & Davalos, 2009). Furthermore, qualitative analysis aids most decisions as it is easier more cost effective to conduct than quantitative methods. The downside of qualitative analysis when compared to quantitative analysis, however, is that it has a lot of uncertainties and information may be less accurate.

## Qualitative risk analysis process

| Qualitative Risk Analysis | Probability of occurrence | Impact of risk | Risk Mitigation strategies |
|---|---|---|---|
| Non-numeric analysis | Often | Severe | Risk acceptance |
| | Not often | Very high | Risk avoidance |
| | Rare | High | Risk transfer |
| | Very rare | low | Risk reduction |

Table 1 The qualitative risk analysis process

## Pension Fund Typology

Pension funds are broadly classified as Defined Benefit (DB) or Defined Contribution (DC). In DC plans, a member's benefits are determined by the sum of contributions made and the investment earnings on the account. The member has a say on what investments their contributions should be put into and the member is able to know the value of their savings at any time. In Defined Benefit plans, the member's benefit is determined by a formular which accounts for the number of years in service, wages earned, and social security benefits a member is entitled to (Bodie, Marcus, & Merton, 1988).

**Risk management in DB pension funds**

Risk management in Defined Benefit pension funds focusses on both measuring and assessing the fund risk and the design, monitoring and evaluation of the funds parameters which are contributions, benefits, and investments in line with the objectives of the fund (Blome, Fachinger, Franzen, Scheuenstuhl, & Yermo, 2007). The main risks affecting DB funds are investment, inflation, and longevity risks while those affecting members include the risk of insufficient assets to cover promised benefits if fund is terminated due to insolvency (Blome et al., 2007).

The goal of risk management in DB schemes therefore should be twofold, firstly to reduce the contributor's cost of pensions and secondly to minimise beneficiary's benefit cut risks. This creates a contribution, asset allocation and risk trade-off to meet the stakeholders' varied objectives. Plan net funding cost minimisation through optimisation of risk adjusted return on assets is the focus of plan sponsors while members have goals that change over time. Members would like to reduce their pension cost, maximise their plan benefit during active years without losing their vested benefits and retired members emphasise benefit security as they have no time to make up the shortfalls. The task remains therefore to create a combination of contribution and benefit policies and strategies of funding and investments that satisfy both the plan sponsors and active and retired plan members (Blome et al., 2007)

**Early Pension Withdrawal**

A study conducted by (The World Bank Group, 2019) pointed out that a well-designed pension system will not only aim to reduce poverty in old age but will cushion income throughout one's lifetime as well. Furthermore, changing demographic trends had caused a shift from DB schemes which placed the obligation for paying retirement income on the government and the employers to DC schemes which placed the obligation on the individual themselves to save for retirement.

The study highlighted a lack of emergency saving and indebtedness as the reason for pre-retirement liquidity. NEST Insights paper (2017) as quoted by (The World Bank Group, 2019) stated that *"high-cost and unpredictable one-off expenses such as the breakdown of a household appliance can cause acute short-term financial hardship for people whose disposable income after essentials is low. In addition, financial shocks among low-income groups can lead to debt spirals which can cause acute financial stress. Any severe or persistent pressure on liquidity can have significant health effects, which can in turn affect productivity and earning capacity…. In an extreme case, one could imagine for example, a short-term financial shock such as the inability to afford a car repair having dramatic knock-on consequences such as loss of earnings and increased debt."*

Although Pension system development has been linked to economic growth, there have been other short comings. The high concentration of investments in bank deposits and government bonds deliver low investments returns which translate into low pension benefits. "*OECD Global Pension Statistics show that around half the assets of pension funds around the world are held in bills and bonds – with the proportion significantly higher in non-OECD countries (at 58.6% of total assets under management (AUM))"* (Morales, Fuentes, Searle, & Stewart, 2017).

According to a study by (Kotecha, Rantanen, Barber, & Georgia Lucey, 2020), retired and non-retired study participants desired financial security which is the ability to pay for bills and food, financial freedom to be able to afford various leisure activities as well as intergenerational transfers which is the ability to financially assist their children as well as the possibility of leaving an inheritance for them in their retirement. With these needs not being met by retirement pensions benefits, members feel they could withdraw their pensions and make alternative investments that could offer them better returns in retirement.

**Risks of early pension withdrawal**

The most obvious risk of early access to pension savings is the risk of inadequate retirement income. This risk may occur even in systems without a direct access link to pension savings through contribution holidays or reduced earning capacities. Members with more education and higher income usually save for retirement while members who withdrawal their pension early are usually from a lower education and income background and are likely to spend these funds on debt repayments (Butrica, Zedlewski, & Issa, 2010). This is supported by (The World Bank Group, 2019) whose study showed that vulnerable people especially those with less education, have no other financial assets and have the least retirement savings have highest rates of withdrawals.

More than half of workers will spend some of their retirement savings if given the opportunity. (Butrica, Zedlewski, & Issa, 2010). Furthermore, the study showed that early pension withdrawals are usually necessitated due to job loses, loss of income, divorce, and home purchases with each of these events increasing the likelihood of a withdrawal by 3 to 10%. The younger workers with low balances are most likely to spend their retirement savings resulting in significant loss to their retirement income. Vulnerable individuals facing various shocks which include the loss of income are likely to withdraw their pension early (Bekbossinova, Oshanova, Khassenova, Alpysbayeva, & Moldasheva, 2022).

Pension savings for this group also constituted a major source of wealth for the lower income workers in the UK who were excluded from financial services such as loans or mortgages hence access to savings was considered necessary. The argument in the study was by consumer interest groups who stated that access to pensions would open low-income workers to pressure from creditors to meet their debt arrears using pension savings. This view caused countries around the world to put in place strict rules around early pension access for example due to limited and inconclusive evidence on the benefits to under saving groups, the UK government did not approve a proposal for early access to pension saving in 2011.

The study by (The World Bank Group, 2019) also supported this argument for extreme cases, it stated that in the face of extreme shocks, limited pensions access can help improve the welfare of individuals. Early access to pensions in some countries in the Pacific Islands which were affected by a natural disaster improved people’s welfare. This could be comparable to the COVID 19 period in 2019 – 2021 when a lot of people lost their jobs or businesses and had no other source of funds.

**Early pension withdrawals in sub-Saharan region**

Early access to pension saving not only has an impact on the members as can be seen in Uganda where early access to pensions had a 2.5% decrease in the interest rate in the 2021/2022 savings year when compared to the previous year (Busuulwa, 2022). Early access to pension can also have an impact on the pension fund. High volumes of withdrawals would lead to an increase in portfolio liquidity. This would restrict investment opportunities in long term instruments reducing the ability of the scheme to generate higher returns through illiquidity premiums (The World Bank Group, 2019). When early withdrawals are a major driver of outflows, early pension withdrawals would have a major impact on pension funds (Morales, Fuentes, Searle, & Stewart, 2017).

A correlation analysis study on the impact of accessing pension benefits before attaining retirement age in Kenya conducted by (WERE, 2011) as quoted by (Murithi, 2015) revealed that an inverse relationship exists between early access to pension benefit and fund financial performance. The study highlighted that Ksh. 2 billion was accessed by members within a period of six months. The researcher indicated that this would affect the pension funds liquidity in the short term, and it was recommended that the Kenyan Government

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takes appropriate measures to mitigate this in the long term.

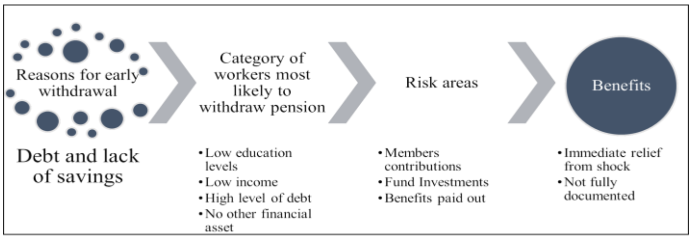


Figure 3 early pension withdrawal areas of risk

Overall, early access to pension savings can lead to a decrease in the interest rate, affect the pension fund's financial performance, and reduce its ability to generate higher returns. It is, therefore, essential for pension funds and policymakers to consider the implications of early access to pensions and devise appropriate measures to mitigate its adverse effects. While early access may be necessary in certain cases, it is crucial to strike a balance between providing access to funds and ensuring the long-term sustainability of the pension fund.

**Knowledge Gap**

The early pension withdrawals in the studies have been in DC schemes, there is clearly limited information on how early pension withdrawals can be implemented in DB schemes which is the focus of this study. Most of the authors have identified debt and lack of saving as a reason for early pension withdrawals but have not highlighted the full benefits of early pension withdrawals. Non have compared the benefits of withdrawal to the effects it would have on the scheme. As Zambia in in the process of reforming the major pension scheme in the country, this gap in the literature must be filled to make the most effective pension reforms.

## METHODOLOGY

This chapter outlines the research methodology employed in this study. It is important to identify and apply the most appropriate methodology for this research to ensure that the research is credible. The research onion by (Saunders, Lewis, & Thornhill, 2016) was used as a guide for the construction of the research framework. The chapter will begin by highlighting the philosophy and research approach used including the strategy justification. This then helps to define the method of data collection and analysis most appropriate for the research. This chapter will also cover all ethical considerations of this research. The chapter is important because it will help us address the aim of this study which is to analyse the risks that arise from early pension withdrawal in Defined Benefit schemes. This helped answer the research questions as well as develop new knowledge on the subject.

**Underlying Philosophy**

An interpretivists paradigm was used for this study. Paradigm in research refers to the researcher's view of the world which informs their interpretation of the research data (Kivunja & Kuyini, 2017).

According to Lincoln and Guba (1985), and Morgan, (2007) as quoted by (Kivunja & Kuyini, 2017), state that research conducted with an Interpretivist paradigm will usually have the following characteristics: " *The admission that the social world cannot be understood from the standpoint of an individual, the belief that realities are multiple and socially constructed, the acceptance that there is inevitable interaction between the researcher and his or her research participants, the acceptance that context is vital for knowledge and knowing, the belief that knowledge is created by the findings, can be value laden and the* *values need to be made explicit, the need to understand the individual rather than universal laws, the belief that causes and effects are mutually interdependent, the belief that contextual factors need to be taken into consideration in any systematic pursuit of understanding*".

The methodology used in the interpretivist paradigm is naturalist. The researcher acts as a participant and data is collected through interviews, texts, discourses, and reflective sessions. Data will be gathered using interviews in this study.

**Research Approach**

The abductive approach which is a combination of the deductive and inductive approach was used in this study. It used where patterns are explained and themes identified from data collected to explore an occurrence to modify existing theory or generate a new theory which is tested from data collected (Saunders, Lewis, & Thornhill, 2016). The deductive was drawn from secondary data on the topic while the inductive is drawn from primary data collected.

**Time Horizon**

This was a cross-sectional study with data being collected between November 2022 and April 2023. Data pertaining to this study was neither collected before nor after this period for this research.

**Research method and Justification**

A mono-method qualitative exploratory case study was conducted because the research aimed to obtain an in-depth understanding of the research problem from key participant's experience and knowledge on the topic and produced findings not arrived at by statistical procedures or other means of quantification. Qualitative research is appropriate for research about organisational functioning, social movements, cultural phenomena interactions between states (Rahman, 2016). A qualitative case study also enables the researcher to explore an intricate phenomenon within it naturally occurring context and reveals multiple aspects of the phenomenon (Rashid, Rashid, Warraich, Sabir, & Waseem, 2019). An exploratory study is valuable because it allows the researcher the freedom to ask open questions to have full insights about a topic (Saunders, Lewis, & Thornhill, 2016).

**Research Strategy**

A case study research strategy was employed in this study. A research strategy is a plan of action the research undertakes to answer the research question and is a link between philosophy and data collection and analysis method. A case study leads to in depth scientific descriptions and theory development by generating insights from a naturalistic context study (Saunders, Lewis, & Thornhill, 2016).

**Sampling frame and sample size**

The participants of the study were selected using purposive sampling because it is appropriate for small samples for example in case study research and helps select participants who will be most informative in answering the research questions and meeting research objectives (Saunders, Lewis, & Thornhill, 2016). The research used the theory of saturation in selecting the number of interviews to be conducted. This ensured that collect data was sufficient for analysis. The interviewees were selected based on their experience and knowledge of pension risk management.

The sample size for the study was 9 which comprised of Senior Staff at the National Pension Scheme Authority.

### Data collection and analysis

The data was collected using one on one, face to face, semi structured interviews and was precisely transcribed and analysed using thematic analysis in NVIVO software to identify the specific themes for the Risk Analysis. A thematic analysis searches for patterns or themes in a coded qualitative data set. A thematic analysis can be used irrespective of whether a deductive or inductive approach, can be used on either large or small data sets and leads to rich descriptions or explanations (Saunders, Lewis, & Thornhill, 2016).

### Reliability, Validity and Generalisability of Research Findings

The various measures and tests that are used to establish reliability and validity of data cannot be applied to qualitative research. There is an ongoing debate about the applicability of validity, reliability, or generalisability to qualitative research. More broadly these terms can apply to qualitative research, validity would refer to the integrity of methods used and how accurately the findings reflect the data. Reliability would refer to the consistency of the data analysis procedure (Noble & Smith, 2015).

Reliability, validity, and generalisation in this study was assured by considering personal biases which may have influenced findings, sampling biases, records were carefully stored and there was a transparent trail of data interpretation. The interview transcripts were also sent to the respondents for validation.

## FINDINGS

The organisation under review is the only public pension scheme covering both public and private employees in Zambia. The research was confined to the Headquarters of the institution in Lusaka province which is where all the Heads of Departments are based who were the targeted respondents for this study.

In its existing form, the organisation has a mandate to collect funds, invest the funds and pay out benefits. It has been in existence since February 2000 and pays out three main benefits which are retirement, invalidity, and survivor benefits.

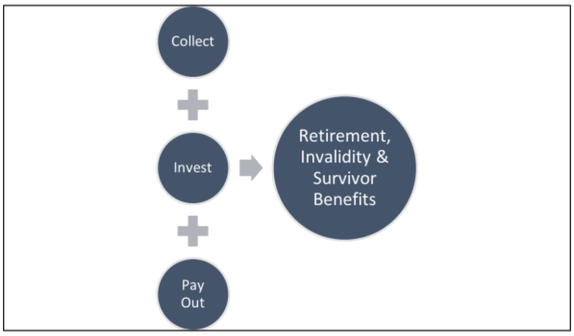


Figure 4 NAPSA's Mandate

### Data analysis overview

This process was inspired by (Braun & Clarke, 2019) thematic analysis process. It began by transcribing interviews, getting familiar with the data, identifying codes, searching, reviewing, and defining of themes and generating findings and finally report writing. A thematic analysis identifies, organises, and reveals patterns across qualitative data sets by providing systematic mechanisms of coding and data analysis which is then linked to theoretical concepts. A data driven approach to coding and theme identification was applied to lessen analyst biasness.

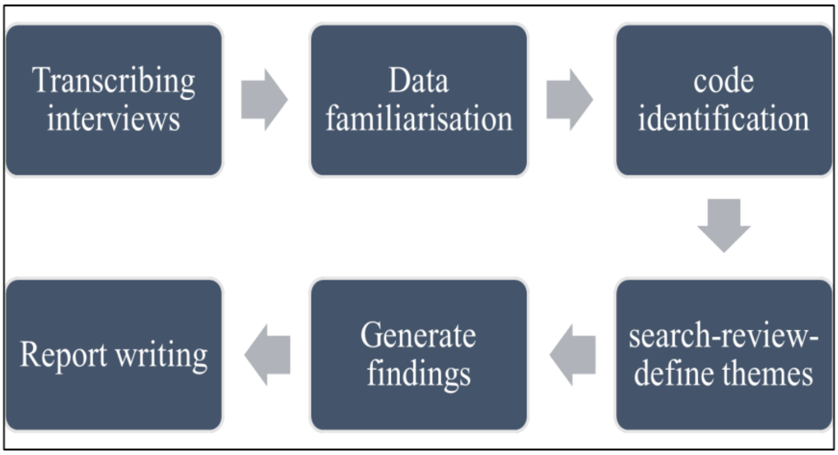


Figure 5 The Thematic analysis process

Additionally, the analysis process for this research ran concurrently with data collection as important notes were taken down during the interviews. The written notes and the recorded data were then transcribed in Microsoft Word and imported into NVIVO 12 software. The software aided the identification of risks by colour coding the data to segregate data that relates to the risks arising from early pension withdrawal, risk impact and finally mitigating strategies.

Various theory building queries were also conducted to aid in the identification of themes. These queries included text search, word frequency, data coding, matrix coding and coding comparison. The themes were then identified and reviewed to ensure they match with existing data. Below is an extract of the attributes of the respondents for this study.

| **Person** | **Duration of Employment** | **Gender** |
|---|---|---|
| **Cases\\Interviewee R001** | Over 20 years | Male |
| **Cases\\Interviewee R002** | Between 5 – 10 years | Male |
| **Cases\\Interviewee R003** | Between 5 – 10 years | Male |
| **Cases\\Interviewee R004** | Over 20 years | Male |
| **Cases\\Interviewee R005** | Over 20 years | Male |
| **Cases\\Interviewee R006** | Over 20 years | Male |
| **Cases\\Interviewee R007** | Between 5 – 10 years | Male |
| **Cases\\Interviewee R008** | Between 5 – 10 years | Male |
| **Cases\\Interviewee R009** | Over 20 years | Male |

Table 2 Attributes of respondents

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As a way of familiarising with the data, a text query was conducted to identify some of the risks that were highlighted by the respondents. These risks are displayed on the word tree diagram below. The word tree aided in the identification of initial codes used for this study.

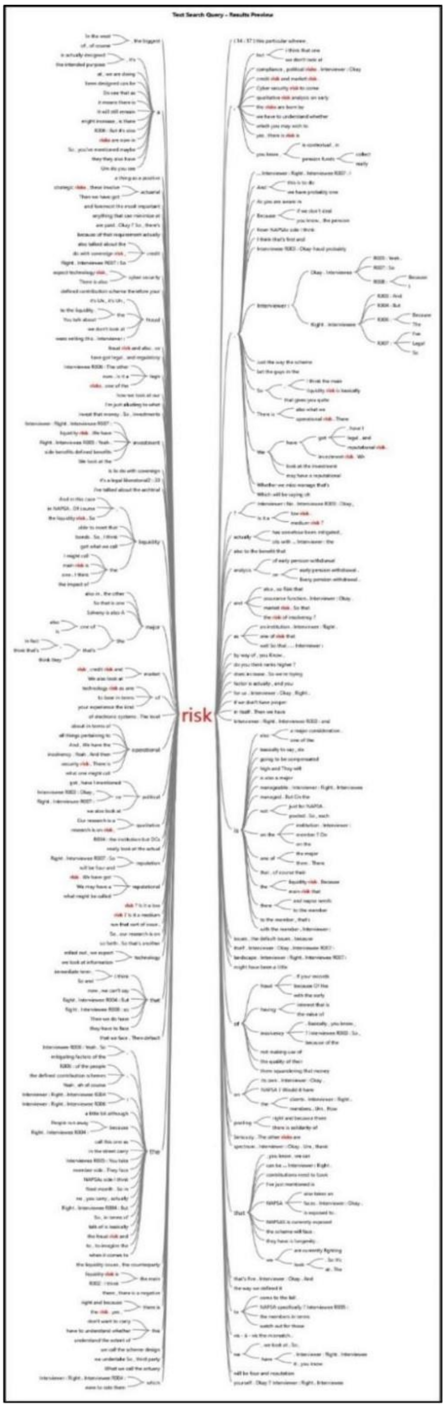

Figure 6 Results of the text query displayed on the word tree diagram.

**Risks associated with early pension withdrawal**

The risks that were identified from the interviews as being associated with early pension withdrawal from the respondents can be broadly categorised as fund risk and member risks as shown in the diagram below. Fund risks are risks that were identified as affecting the Scheme while member risks are risks that were identified as affecting the Members of the Scheme.

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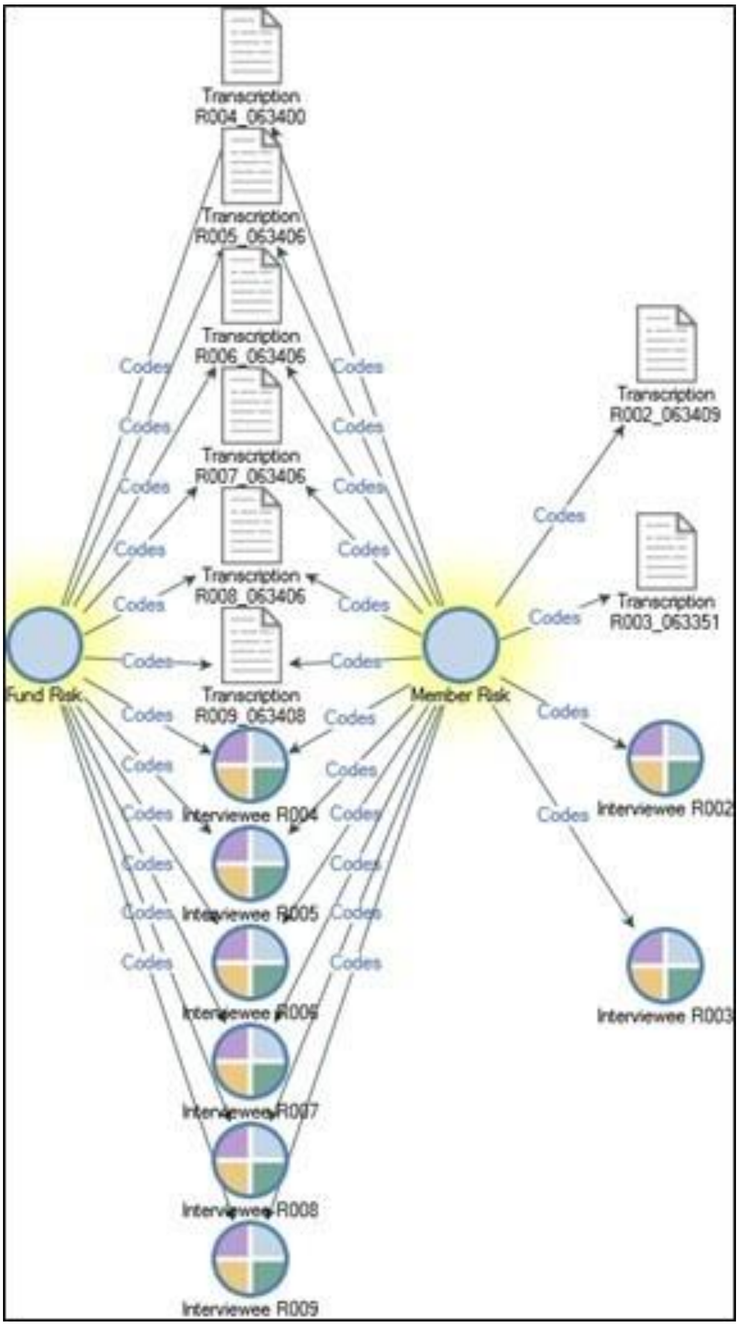


Figure 7 Comparison diagram of fund risk and member risk

| Broader Category | Analytical Node 1 | Analytical Node 2 | Analytical Node 3 |
|---|---|---|---|
| Fund risk | Actuarial Risk | | |
| | Investment risk | Liquidity risk | |
| | Operational Risk | Fraud risk | Identity fraud risk |
| | | Technological risk | |
| | | Reputational risk | |
| | Political risk | | |
| Member risk | Benefits | Early withdrawn benefits | |
| | | Future benefits | |

Table 3 Qualitative data analysis code list

**Fund risk**

Various risks that can affect the scheme due to the early pension withdrawal that were identified by the respondents included Actuarial Risk, Investment risk, Operational risk, and Political risks.

**Actuarial Risk**

Actuarial risk refers to the risk associated with the long-term sustainability of a pension fund, considering various factors such as the existing contribution rate, investment returns, and demographic trends among others. The early pension withdrawal scheme can increase the actuarial risk in two main ways. Firstly, the demand for liquidity caused by the early pension withdrawal may affect the fund's ability to meet its long-term obligations, particularly if the withdrawal requests exceed the expected levels. This can lead to a reduction in the fund's assets and a higher risk of default on its obligations, which can impact the fund's long-term sustainability. Secondly, the early pension withdrawal scheme may bring forward the breakeven point, which is the point at which the fund's assets are sufficient to meet its obligations. This can happen if the withdrawals reduce the size of the fund's assets to a level that cannot generate sufficient returns to meet its obligations. This can lead to the fund's assets being depleted faster than anticipated, which can impact its long-term sustainability.

*"…what I mean by breakeven point, is the point at which the scheme may not be able to sustain itself given contribution rate that would have been predetermined…" [Interviewee R002]*

*"…So, you find that by having things like early withdrawal come into play, you are affecting the period at which this breakeven point may come in the future. So, for instance, assume that the latest actuarial evaluation predicted that the breakeven point for NAPSA was maybe say 2034 or 2035, the coming in of this early withdrawal may affect this because it may bring it closer because they'll be need for liquidity, to pay those benefits…" [Interviewee R002]*

*"…In the short term it brings forward the break-even point because you are required to pay more now…" [Interviewee R005]*

**Mitigating strategies**

An upward revision of the contribution rate may be necessary to mitigate the actuarial risk associated with the early pension withdrawal. However, an increase in the contribution rate may be perceived as unfavourable by members, who may prefer to have greater control over their funds.

*"…Then it will become relevant for us to ask questions, like Should we be increasing the contribution rate?" [Interviewee R007]*

*"…so, some of the things that can aid to push that break even period further into the future could be things like increasing the contribution rates say from the current 5% to maybe 7.5% because it means that the buffer of money that is left after the early withdrawal increases…" [Interviewee R002]*

NAPSA may need to explore alternative measures to mitigate the actuarial risk, such as: Diversifying the fund's investment portfolio to increase its returns and reduce dependence on contributions, exploring alternative sources of funding, such as government grants or private investments, enhancing risk management practices to monitor and manage the fund's exposure to different types of risks, promoting financial education and literacy among members to encourage responsible use of their pension funds.

By taking these measures, NAPSA can mitigate the actuarial risk associated with the early pension withdrawal scheme and ensure the long-term sustainability of the fund.

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### Investment risk

The respondents addressed this risk in terms of the long-term mandate of the scheme. In its current design, the scheme pays out a benefit only in three eventualities, retirement, invalidity, or death. The early withdrawal therefore could limit the amount of funds that the scheme has available to put into long term investments due to the need for liquidity to pay the benefits that would arise. The respondents reported however, that the early withdrawal could cause a risk to investments in the initial years, but this is expected to stabilise and increase in the later years after more people have made a claim on the early withdrawals.

*"…So instead of growing with a normal growth of 19 to 20 to 25%, it will actually reduce to about 8 – 10%. So that is the immediate impact of early withdrawals…" [Interviewee R001]*

*"…and you know NAPSA has to invest these funds for them to grow. So, it means they may have to look at Pulling back some of the resources from where they have been invested to be able to meet this obligation…" [Interviewee R008]*

*"…So, the pre-determined withdraws now will intel that we kind of scale down in terms of investing in the long term and we start looking at the short and the medium-term horizon because we need to create the much-needed liquidity to cover those pre-retirement benefits…" [Interviewee R001]*

*"…So, I think in the short term, there might be that turbulence in terms of meeting this, but I think long-term, from NAPSA side, it's likely to stabilise all things being equal…" [Interviewee R008]*

*"… if the uptake by members is high, in the initial years, there'll be a huge out flow of funds, yes, but in the long run, it will become cheaper for the Authority because the quantum of the benefits that will be paid in the latter years will be lower…" [Interviewee R009]*

### Liquidity risk

The need for liquidity to pay out benefits can affect the funds available to invest in long-term assets, which generate the most interest. Additionally, the availability of these funds to pay benefits at a particular point in time when members demand for payment can also create liquidity risk.

*"…. I think the main risk is the liquidity risk. Because you know, the pension scheme invests its money with the view that they will be pay it at the certain predetermined time. but due to this early withdrawal will mean that NAPSA may be forced to invest only in short term investments such as maybe treasuring bills and they may move away from longer financial instruments like government bonds…" [Interviewee R002]*

*"…So, in our case now that we are talking of a partial withdraw, clearly certain dynamics come into play. The first one is what I might call the liquidity risk. So, liquidity risk is basically to say, do we have enough funding? To pay the benefits as they fall due…" [Interviewee R003]*

### Mitigating Strategies

To manage liquidity risk, NAPSA should have adequate cash reserves to meet its short-term obligations, including the payment of benefits. This can be achieved by investing in highly liquid assets such as money market funds, short-term government bonds, and other highly rated securities. NAPSA should also conduct regular cash flow projections to identify potential liquidity shortfalls and plan accordingly. This can involve setting aside funds in advance of expected benefit payments or negotiating credit facilities with financial institutions to provide additional liquidity if needed. Another strategy to manage liquidity risk is to diversify the investment portfolio to ensure that there is a mix of highly liquid assets and longer-term investments that

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provide higher returns. This can help to balance the need for short-term liquidity with the need to generate sufficient returns to meet the Scheme's long-term obligations.

*"…now we will need to kind of shift our thinking and go into the active kind of investment strategy where we will be entering markets which are active so that we can grow the much-needed liquidity in a short time and that will meet part of the pre-retirement and also assist in terms of growing the portfolio…" [Interviewee R001]*

By managing liquidity risk effectively, NAPSA can ensure that it has sufficient funds to pay benefits when they are due, while also investing in assets that provide the highest returns over the long term.

**Operational Risk**

This risk focused on the day-to-day operations of the scheme and how capable the Scheme is service ready to roll out this benefit successfully. This was broken down into fraud risk, technological risk, and reputational risk.

*"…The fourth one is probably what one might call operational risk. And this is to do with our readiness to provide the service. So, do we have systems in place to provide this service? Do we have the people? Are we likely going to have a situation where there will be so many queues?" [Interviewee R003]*

**Fraud risk**

The risk of fraud is a significant concern for NAPSA particularly in relation to the early pension withdrawal scheme. Poor record keeping and identity theft are some of the risk factors that can lead to fraudulent activities within the Scheme. If not managed properly, this can lead to financial losses for the Scheme and damage to its reputation.

Poor record-keeping can create opportunities for fraudsters to submit false claims or manipulate data to obtain benefits to which they are not entitled. This can be particularly challenging for the early pension withdrawal scheme, which may involve a large number of claims that need to be processed quickly and efficiently.

*"…The second that you can talk of is basically the risk of fraud. If your records are not properly kept and you have got, you know, challenges of your records then, you know, it becomes a big challenge for you to pay because are you going to pay the right person? Or is going to be a wrong person that you're going to pay? So, that becomes a big challenge in terms of managing, you know the applications that are coming through. So, you have to be mindful of who is in front of you? Is this a real person who is supposed to be claiming or is it a different person?"*

*[Interviewee R003]*

Identity theft is another risk factor that can lead to fraudulent activities within the Scheme. Fraudsters may use stolen identities to create false claims or manipulate data to obtain benefits fraudulently. This can be particularly challenging for NAPSA, which needs to ensure that it has robust identity verification processes in place to prevent such fraudulent activities.

*"…So, um they also have a risk to watch out for those who want to do identity theft…" [Interviewee R008]*

**Mitigating strategies**

To mitigate the risk of fraud, NAPSA should implement robust internal controls, including regular fraud risk assessments, staff training on fraud prevention measures, and independent audits. NAPSA should also invest in robust technological infrastructure to ensure secure data storage and transmission, as well as identity verification processes that are robust and efficient. By doing so, NAPSA can reduce the risk of fraudulent activities within the Scheme and ensure that benefits are paid only to those who are entitled to them.

**Technological Risk**

NAPSA's investment in e-platforms is a positive move towards improving the efficiency and accessibility of pension services. However, it also exposes the Authority to various cyber security risks, such as data breaches, hacking, phishing, and malware attacks. These risks can lead to the loss or theft of sensitive personal and financial information, disruption of services, reputational damage, and financial losses.

*"…So, we look at information technology risk as one of risk that NAPSA is exposed to…" [Interviewee R007]*

*"… if the fraudsters get hold of our database for instance, they know, this is ABCD, they can use that information to their advantage, but it goes back to how you safeguard your information…" [Interviewee R007]*

**Mitigating strategies**

To mitigate these risks, NAPSA should prioritise cyber security measures that protect the confidentiality, integrity, and availability of the data and systems. This may include:

Conducting regular risk assessments to identify and prioritise cyber security risks and vulnerabilities, developing and implementing robust policies and procedures for cyber security, including password management, access controls, data encryption, and incident response, providing regular cyber security training and awareness programs to employees, stakeholders, and members, using reliable and up-to-date anti-virus, anti-malware, and firewalls to prevent and detect cyber-attacks, conducting regular penetration testing and vulnerability assessments to identify weaknesses in the systems and applications, developing and testing a disaster recovery and business continuity plan in case of a cyber security incident, engaging with reputable and experienced cyber security consultants and service providers to advise and support the Authority's cyber security efforts.

By adopting these measures, NAPSA can better protect its e-platforms and the sensitive information of its members, while ensuring the continuity and efficiency of its services.

*"…technology, of course it's continuous improvement in terms of enforcing the latest technological advancement…" [Interviewee R008]*

*"…The Authority is also trying to strengthen controls around the entire system because we know that, with the deployment of electronic systems. The level risk does increase. So, we're trying to tighten security against cybercrime…" [Interviewee R009]*

**Reputational risk**

The early pension withdrawal scheme, if not managed effectively, can expose NAPSA to reputational risks in two main ways.

Firstly, if the influx of clients claiming the early withdrawal benefit exceeds the capacity of the Authority to manage, this may result in delays and errors in processing the claims. This can lead to frustration and dissatisfaction among the members, who may lose confidence in the Authority's ability to provide efficient and effective services. The negative publicity and criticism that may arise from such incidents can damage the Authority's reputation and erode public trust.

Secondly, if the retirement benefits of members who claim the early withdrawal are significantly reduced at retirement, this can also affect the confidence that members have in the Authority's ability to secure their social and economic well-being. This can lead to negative perceptions about the Authority's fairness and transparency and may result in members seeking alternative pension options. This can have long-term implications for the Authority's sustainability and growth.

*"…and that probably turns into what might be called reputational risk. Because if we don't deal with the influx of the people who will be becoming through because we don't have processes, we don't have systems, we don't have people which are all things pertaining to operational risk. We may have a reputational risk…" [Interviewee R003]*

*"…in case somebody retires, and they did not make use of this money, they will be saying NAPSA is not living up to its promise…" [Interviewee R006]*

**Mitigating strategies**

To mitigate these reputational risks, NAPSA should prioritise the effective management of the early pension withdrawal scheme. This may include: Ensuring adequate capacity and resources are in place to manage the influx of clients and process claims efficiently, implementing robust quality assurance measures to ensure the accuracy and completeness of data and information used in the processing of claims, providing regular and transparent communication to members about the status of their claims and any updates or changes to the scheme, conducting regular monitoring and evaluation of the scheme to identify areas of improvement and address any issues or concerns raised by members or stakeholders, ensuring that the retirement benefits of members who claim the early withdrawal are reasonable and fair, and that members fully understand the implications of their decisions.

*"…So that if there is a huge uptake, we do not have any challenge in the disbursements. And, given the anticipated increase in the uptake, the authority is trying to develop, or is developing a robust payment system that will be largely electronic…" [Interviewee R009]*

**Political risk**

There have been calls from the public to make reforms to NAPSA which is the driving factor for the early pension withdrawals. In an effort to be responsive to the various calls by the public, the government instituted legislative changes that addressed the needs of the public. As at the time of writing this thesis, there was The National Pension Scheme (Amendment) Bill of 2023 which was at Third reading stage.

*"…this is a policy directive…" [Interviewee R002]*

*"…So, it responds to that, the government came up with a policy to change the law or amend NAPSA Act…" [Interviewee R008]*

The National Pension Scheme (Amendment) Bill of 2023 is a step towards addressing the concerns of the public regarding NAPSA and early pension withdrawals. The bill aims to introduce various amendments to the National Pension Scheme Act of 1996, which governs the operations of NAPSA.

One of the proposed amendments includes allowing members to access a portion of their savings early. This proposed amendment is a step towards making NAPSA more responsive to the needs and concerns of its members and the public.

*"……to this question and even a third dimension, okay? Let me begin with the third dimension. The third dimension has to do with the objective of the sponsor, okay? What does the sponsor want to achieve?" [Interviewee R003]*

**Mitigating strategies**

It is important to ensure that the proposed reforms are implemented effectively and efficiently, with adequate resources and capacity building for NAPSA and its stakeholders. Regular monitoring and evaluation of the reforms will also be crucial to ensure their impact and sustainability.

*"…so, there's that possibility that this benefit once it is rolled out, might have a positive impact on the economy…" [Interviewee R007]*

**Impact to Fund**

The fund has been in existence for only 23 years. It was viewed by the respondents that in this time however the fund has grown. The biggest impact that the respondents highlighted was on the long-term investments of the fund which may be impacted especially by the volume of members claiming the benefit.

*"…I think the other comforting part is when we study the actual report, even the current one, it still provides that the authority is still young. It hasn't reached the maturity. Even the condition that it can be adjusted. So that gives us some headroom to actually enter into the various investments that are able actually even to impact on the growth of digital portfolio…" [Interviewee R007]*

*"…if we are saying 80 percent of people come and withdraw some of their money, of course, that will Significantly affect the scheme, but I suppose that the time of implementation, that's when we can really be able to analyse the impact…" [Interviewee R002]*

*"…the impacts on the scheme, does it have an impact on this this scheme? Of course, it slows the scheme accumulation of fund reserves…" [Interviewee R005]*

The respondents stated that the early withdrawal would impact the scheme in the initial years of the benefit roll out, but it may not affect the scheme in the long term. On the contrary it was highlighted that the early withdrawal would actually help improve the Authority's compliance rate of around 41% and increase collections as most people especially the younger people would want to be able to benefit from this product.

*"…So, we are still convinced that in the long term the portfolio still will bounce and will actually pick up even at a higher rate than the way it was growing…" [Interviewee R007]*

*"…but I think that because you would have paid some of the liabilities upfront then it's also possible that it's got the effect of reducing your liabilities on the scheme because there is early payment of those liabilities, and you don't allow them to accumulate…" [Interviewee R005]*

*"…so, the impact I think it's, it's low, it's not something that We can say, we could have been worried if it was medium, and I don't think we could have reached this point of where the bill is now at its third reading…" [Interviewee R007]*

**Member risk**

In the provision of the early withdrawal benefit, the members of the fund assume the most risk as highlighted by the respondents. The risk is to their benefits, and this can be categorised as risk to early withdrawn benefit and also risk to future benefits. In the Defined Benefit formular used by NAPSA, a member's pension benefit is affected by the number of years that they have contributed to the scheme.

*"…So, when actuaries are making up that formula, they put into account, well they make several assumptions and some of the assumptions are that an individual would contribute for a certain number of years. But if that individual along the way withdraws part of their money, that affects how much they would get…" [Interviewee R002]*

**Risk to early withdrawn benefit**

There is a risk that some members may use the funds for consumption purposes rather than investing them for their long-term financial security. This can lead to a situation where members exhaust their savings prematurely and are left with insufficient funds to support themselves in retirement. In addition, there is a risk that some members may invest the funds in business opportunities they have no experience in or are not well-informed about. This exposes them to the risk of fraudsters and scams, which can result in the loss of their savings.

*"…so, I think that's also another area, some might go into investment ventures without, you know, really analysing because they've got money…" [Interviewee R008]*

*"…Yeah. So, the risk of them squandering that money is high. And of course, even just the low literacy levels for some good percentage of our members…" [Interviewee R008]*

**Mitigating strategies**

To mitigate these risks, it is important for NAPSA to provide members with education and guidance on how to use the early pension withdrawal benefit wisely. This may involve providing information on investment strategies, financial planning, and risk management. It may also involve working with external partners, such as financial advisors and consumer protection agencies, to help members make informed decisions about how to use their funds.

*"…but as it evolves, we want to embark on so many sensitisations such as financial interests…" [Interviewee R006]*

*"…the second mitigation that is possible is for members to invest in the second-tier schemes. Now, second tier schemes are in-house schemes…" [Interviewee R005]*

*"…or voluntary contribution or supplementary contribution…" [Interviewee R004]*

In addition, NAPSA may consider implementing safeguards to prevent members from using the funds for consumption purposes. For example, they may require members to provide evidence that the funds will be invested in a legitimate business opportunity or asset before approving the early pension withdrawal. They may also provide members with access to financial counselling services to help them make informed decisions about how to invest their funds.

*"…well, I think the important thing is that not everyone should not be able to qualify for this early withdrawal. There should be a criterion. So, for instance, maybe you could say this benefit is only open to people who have contributed to a scheme for a minimum number of months. Or have contributed to the scheme, up to a certain amount of money…" [Interviewee R002]*

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### Risk to future benefits

It is important to understand that withdrawing an early benefit from a Defined Benefit scheme can have significant long-term consequences for a member's pension benefits. One of the main risks associated with early withdrawals is the potential for reduced benefits in proportion to the withdrawn benefit, which could result in a significant impact on a member's later pension benefits.

In the case of NAPSA's Defined Benefit scheme, low contributing members whose calculated pension would be low are uplifted to the minimum pension as prescribed by NAPSA in that specific year. This is an important safety net for members who may not have contributed enough to the scheme to receive a higher pension benefit. However, if these members choose to withdraw their benefits early, they will lose this safety net and may end up with significantly lower pension benefits in the future.

### Mitigating strategies

It is therefore important for members to carefully consider the long-term consequences of early benefit withdrawals and to seek advice from a financial advisor or pension specialist before making any decisions. Additionally, employers and NAPSA can play a key role in educating members about the risks associated with early withdrawals and providing them with the information and support they need to make informed decisions about their retirement savings.

*"…because when they withdraw this money, and they use it for consumptive purposes. It means it will impact their livelihood later…" [Interviewee R009]*

*"…Even the pensions, the value of the pension will be lower. To the extent of the amount which the people will withdraw…" [Interviewee R009]*

*"…clearly because what is going to happen is, I mean, if you had for arguments sake, a 100 thousand on your account and then you withdraw 30 thousand. At a point now, when you are going to begin receiving your, you know, pension, it will not be the same as it would have been, if you had not withdrawn…" [Interviewee R003]*

### Impact on members

The early withdrawal benefit can have both positive and negative impacts on members. On the positive side, it may increase members' awareness about social security and the importance of saving for retirement. However, the negative impact is that the early withdrawal may reduce the future benefits of members if the withdrawn benefit is not used for investment purposes or if it is used to invest in risky ventures. Ultimately, the success of the early withdrawal benefit will depend on how well it is applied by individual members, and this presents a significant risk to the future benefits of members.

*"…So, we expect to see more increased interest in NAPSA by the young generation, because they might want to qualify for this particular benefit. So, in wanting to put away with a huge amount, they will collaborate with the institution in enforcing compliance. I think that's the positive aspect of this proposed benefit…" [Interviewee R009]*

*"…so, in essence the impact is largely dependent on how effectively the amount which is withdrawn is applied…" [Interviewee R009]*

*"…So, the impact of this is that if one draws this early withdrawal pension and they do not apply the withdraw into a productive investment. What they will get at the end of their working life or when they become eligible, or what their beneficiaries will get will be lower than what they would have gotten, if they're not withdrawn…" [Interviewee R009]*

## CONCLUSIONS AND RECOMMENDATIONS

This research has highlighted various risks that arise from early pension withdrawal in Defined Benefit schemes. The risks that have been identified as arising from early pension withdrawal are those that affect the fund and those that affect the members. The need to understand these risks and their impact is cardinal for the development of effective strategy and management of pension reforms. The literature highlighted that members with the lowest education and high debt levels are most likely to withdraw their pension early and that the members are at risk of suffering the highest impact of the early withdrawals. This study therefore recommends that a moral obligation is placed on NAPSA to ensure that members make informed decisions as they withdraw this benefit as the provision of adequate retirement benefits lies within their mandate. A summary of identified risks, their probability of occurring and their impact is highlighted in the tables below.

**Identified Risks**

| **Fund/ Members** | **Risk** | **Risk Description** |
|---|---|---|
| **Fund** | Actuarial | This refers to the risk associated with the long-term sustainability of the fund, given the existing contribution rate and the demand for liquidity that the early pension withdrawal may cause. |
| | Investment | The early pension withdrawal benefit may lead to a reduction in the size of the fund's assets, which can impact the fund's investment performance and returns. This can lead to a higher risk of investment losses and reduces the fund's ability to meet its long-term obligations. |
| | Operational | The early pension withdrawal may increase the operational risk faced by NAPSA, particularly if the influx of claims exceeds the capacity of the Authority to process them efficiently. This can lead to errors and delays in processing claims, which can impact the satisfaction and confidence of members. |
| | political | The early withdrawal benefit can also expose NAPSA to political risks, particularly if there are changes in government policies or regulations that affect the scheme. This can lead to uncertainty and volatility in the fund's operations and investment strategies, which can impact its long-term sustainability. |
| **Members** | Early withdrawn Benefits | The early pension withdrawal can expose members to risks such as fraudulent investments or consumptive purposes instead of investments. |
| | Future Benefits | Members future benefits are at most risk of being impacted by the early withdrawn benefit it lowers the retirement benefits. |

Table 4 Description of identified risks.

**Probability and Impact matrix**

| FREQUENCY OF OCCURANCE | IMPACT OF RISK | | | |
|---|---|---|---|---|
| | Low | High | Very High | Severe |
| Not likely | | | | Actuarial |
| Somewhat likely | | Operational risk | Political | Investment risk |
| Very Likely | Early withdrawn Benefits | | | Future benefits |

Table 5 Probability and impact matrix

**Recommendations**

These are recommendations based on the findings of the study. Conducting mass sensitisation and financial literacy programs would help members to make informed decisions about the early withdrawal benefit and plan effectively for their retirement. The promotion of secondary private pension schemes would also help to increase the availability of finance to members. Implementing measures to secure information against fraud, especially identity fraud, is important for the protection of members and the credibility of the scheme. Finally, conducting a follow-up study and actuarial evaluation after the benefit has been rolled out would provide insights into the actual impact on the fund and how members are using the withdrawn funds, which could inform future policy decisions.

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