

Social Protection: National strategy to provide for the elderly

While the sickly National Health Insurance implementation has dominated recent news, questions on South Africa's approach to old age income have been asked for decades, with little progress on the fundamentals. How do countries care for their senior citizens and where is South Africa in this process? The bottom line is that we have some significant gaps in our approach to the problem. The most likely to suffer as a result: those in the middle.

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If you were tasked by your president to determine the best way to provide some form of income security for your elderly citizens, how would you do it?

Would you promise them income grants? You need to fund them. Would you require all workers to pay a tax? That solves the funding problem but may result in more recipients than workers in future? Would you insist that workers are members of retirement funds or make contributions to individual arrangements? Instead, you could encourage but not force them to do so, but how? Or would you establish a national fund to which they make such contributions today in return for benefits at old age?

These approaches have all been tried. A scan of systems across the world's countries shows a remarkable variety of possibilities.

A modern phenomenon

National social protection for old age—some prefer the expression *social security*—had its stirrings in the late 1800s, but it grew into prominence after the Great War. The International Labour Organization, a tripartite body established in the League of Nations at the Treaty of Versailles, began to build a framework for a set of global social security norms.

Old age provision is one of these norms. Other global organisations have contributed to robust debate regarding such a framework, but it is broadly accepted that a healthy national system has four key elements:

1. **Unfunded pension:** a flat grant, or income linked to earnings at retirement, paid to all eligible elderly, that is funded out of tax revenues or general government budgets, not from a pre-existing pool of assets.
2. **Mandatory, funded pension:** an income after retirement based on a formula linked to earnings that is funded by contributions, linked to salary, paid by all workers.
3. **Supplementary, work-based saving:** a company- or industry-based fund into which workers pay contributions in return for retirement benefits, based either on a formula at retirement (defined benefit) or on the level of accumulated saving at that date (defined contribution).

4. **Voluntary individual saving:** any other arrangements that workers may use to save for retirement.

Governments usually such saving by providing some form of incentive, usually in the form of tax breaks. This is often extended to the mandatory part of the system, softening the effect of the compulsion.

Naturally some systems are more liberal than others. Generous benefits must be funded, though, usually through higher contributions, what some prefer to call social security taxes. Determining what constitutes a good system is not easy, but several excellent papers have demonstrated that arguments in favour or one element or another are frequently spurious. In other words, consider the interests or bias of the underlying party when assessing their reasoning.

Where is our country in this framework?

South Africa provides decent social grants (item 1) that go a long way to supporting not just recipients but extended families. These are unfunded, though, so we need to keep an eye on the cost of these grants.

We also have a sophisticated financial sector with a range of occupational (item 3) and individual (item 4) arrangements. The governance and cost of these funds and products nevertheless need constant vigilance.

The real problem is that we do not comply with item 2. Now you may feel compelled to contribute to your employer's pension fund, but this is not a national mandate. Furthermore, should you resign, you have access to (most of) your pension saving. Substantial evidence exists that resigning workers are taking advantage of this access, seriously undermining their old age security.

Why do we need a mandate? Evidence consistently shows that we are notoriously bad at making short-term sacrifices for long-term gain. Unless we are told to save, in other words, we typically don't. Policymakers in most countries have taken the view that the mandate is a necessary evil. The mandate also helps governments to meet other goals such as risk-sharing or redistribution from the wealthy to the poor.

South Africa's recently implemented two-pot system is a creative way to force an element of durability to our saving, but it was needed because we chose not to address more decisively the question of compulsion. Desperate as the circumstances of most South African households may be, things are not going to improve if we do not recognise the looming difficulties of old age and take appropriate action to prepare for that now.

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