



# Insights and investment solutions magazine

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## Spring 2020

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# Welcome

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In this edition of Insights and investment solutions magazine, read the latest market update based on the highlights across the Australian market over the past month.

We look at why super has decreased and we share insights into what you can consider if you're retiring this year.

Until next time – happy reading.



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# Market update

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Over the past month, varying economic results were reported throughout the world. While the hunt for a successful COVID-19 vaccine continues, Governments and central banks are focusing on new and additional forms of stimulus and relief, to support the dire economic state of many nations at present.

The Westpac-Melbourne Institute Consumer Sentiment Index fell 6.1% to a reading of 87.9 in July, the first decline after rising for two straight months. While July's reading was 16.2% higher than the record low in April, the index remains 8.0% lower than pre-pandemic levels. Concerns over rising cases of COVID-19 in Victoria were largely behind the deterioration in overall sentiment. With daily infections surpassing 700, Victorian state borders were closed with Greater Melbourne finding itself facing Stage-4 restrictions. Meanwhile, NSW is implementing softer restrictions for weddings, funerals and venues as well as strongly encouraging the voluntary use of masks when in public.

Wage data is expected to show a 0.4% increase in the June quarter and annual growth is predicted to slow from 2.1% to 2.0%. Furthermore, labour force data is likely to reveal a 40,000 increase in employment throughout the month of July, following the 210,800 surge in June. The increase in employment failed to prevent the unemployment rate rising from 7.1% in May to 7.4% in June, the highest since November 1998. The lift was a result of a large proportion of people returning to the workforce. The participation rate jumped from 62.7% in May to 64.0% in June. Consensus is that the July unemployment rate is expected to reach 7.8%, propped up by an increase in the participation rate to 64.4%.

The government provided an update to budget expectations during July - some 'eyewatering figures' (as Treasurer Josh Frydenberg appropriately labelled them). At the time of the December 2019 Mid-Year Economic and Fiscal Outlook, the government forecasted a AU\$5 billion surplus for 2019-20 and a \$6.1bn surplus for 2020-21.

The deterioration has been sharp and fast. The Federal Government have announced an underlying cash deficit of -AU\$85.8 billion (4.3% of GDP) for 2019-20. The fiscal deficit is expected to rise to -AU\$184.5 billion in 2020-21 (9.7% of GDP). The 2020-21 deficit will be the largest on record, with records starting in 1970. The forecast for Australia's economic contraction in 2020 has been upgraded from 4.0% to 4.2%. The extensive policy measures to support

the economy through the impact of this pandemic have accounted for the bulk of the deficit. Additionally, a heavy decline in economic activity and subsequent loss of employment have resulted in less tax revenue and higher levels of required welfare payments.

The Federal Government also announced the extension of both the JobKeeper and JobSeeker programs over July. JobKeeper has been extended to the end of March 2021, with companies needing to reapply and meet the revenue test every quarter. The new model adds a tiered payment approach, with provisions made for full-time and part-time (less than 20 hours weekly) workers. The new payments are \$1,200/\$750 and \$1000/\$650 for the December and March quarter, respectively. The renamed 'JobKeeper 2.0' that will come into effect at the end of September 2020 will cost an additional AU\$16 billion. Additionally, 'JobSeeker 2.0' will reduce the coronavirus unemployment supplement from \$550 to \$250 per fortnight. There is also a mutual obligation to accept jobs when offered a position. This extension comes at a cost of AU\$3.8 billion. Other support packages were announced over July with the Australian Banking industry announcing that loan deferrals could be extended for up to four months for eligible borrowers. Additionally, the stamp duty exemption in NSW for first home buyers was relaxed, with an increase in the threshold from \$650,000 to \$800,000. Victoria's premier also announced a AU\$534 million Business Support package, which includes a \$5,000 grant to support more than 80,000 eligible businesses in response to the stage 4 lockdowns.

While foreign policy has not been a focus of Australia during the past few months, the Foreign and Defence Ministers have travelled to Washington D.C for national security discussions at the AUSMIN summit. Discussions included Australia's response to the growing threat of China's foreign interference and treatment of Hong Kong citizens.

# How long will my super take to recover?

COVID-19's impact on global stock markets has seen many investors' superannuation balances fall, causing concern and begging the question – why has my super decreased and when will it recover?

If you've checked your super balance recently, chances are it's lower than it was at the start of the year. That's because the value of the major share markets has fallen this year, due to investor concerns about the impact of COVID-19 on the world's economies.

## The share market

Share markets have been volatile since the Australian economy reached an all-time high of 7199.79 points in February 2020. According to Canstar research, the value of the local share market declined by 20 per cent in March but rose by 8.1 per cent in the first two weeks of April alone. In the decade before the market's February high, the market's average annual return was 7.86 per cent.

As this shows, by their nature, markets rise and fall. This means, if you're a long-term investor, like most people with superannuation are, short-term market movements may not be so important.

## Diversification is essential

Diversification is one of the most important factors that helps investors ride through market cycles. This is the concept that by investing in a basket of assets, investors gain exposure to different asset classes – shares, property and bonds, for instance – and may be more able to ride out market cycles and reduce the impact of volatility affecting different parts of the portfolio.

It's also important to be diversified within asset classes. For example, a portfolio of shares will include companies in a range of industry sectors such as banking, mining, consumer goods and transport. Having a diversity of asset classes and industries in a portfolio, in this case, might also help to ride out the market cycle.



### **Time until retirement is key**

As a rule, the further out from retirement you are, the more risk your portfolio may be able to take. This is because most investors need to absorb some level of risk to generate the return they'll need to grow their retirement savings. Nevertheless, it's still important to have some exposure to risk even when nearing and in retirement. An example of this is, if you're in retirement and your portfolio is invested in cash, you have a smaller opportunity to grow a nest egg over time. But if a portion of your portfolio, even a small one, has some risk attached, you have the potential to generate some return even in retirement. This is important especially as we are living longer, which means our retirement savings have to last longer as well.

### **It's impossible to time the market**

It's easy to think it's possible to pick the bottom and top of the market. But in fact, it's only possible to understand when the peak and trough of the market have been reached once those milestones have passed.

This means it can be very risky to try to sell your investments at the top of the market and buy back in when you think shares are at their cheapest. Missing the top of the market can mean missing out on the gains to be made at this point.

Similarly, if you miss the bottom of the market, you may miss out on a subsequent upswing. Worse, if you sell when markets are at a low point, you will crystallise your losses.

Taking all this into consideration, it's important to be invested in the market through different cycles. That way, chances of missing out on the gains you can achieve when markets are at their peak are lower, as well as not locking in your losses when markets have hit the bottom.

It's impossible to be able to say when your retirement savings will be back at the levels they reached at the start of the year. What's important is to be diversified, have some level of risk in your portfolio and ensure your retirement savings are being managed by a team that has a good track record of helping investors grow their retirement savings over time.



# Five things to consider if you're retiring this year

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2020 has seen people make big changes in their lives – cancelling travel arrangements, dealing with unemployment or home-schooling children. And the current market downturn certainly hasn't helped those considering retiring this year.

But whenever you're approaching retirement, you should think about how to protect your nest egg over the coming years. Ensure your retirement strategy is still the right one for your circumstances, whether that's how you're invested, ways to create an income stream or eligibility for the Age Pension.

We've put together a list of five things to consider if you're retiring this year.

## 1. Remember the 10/30/60 rule

The 10/30/60 rule suggests your retirement income comes from three sources<sup>1</sup>.

- 10% from money you saved during your working years.
- 30% from investment returns before you retire.
- 60% from investment returns during your retirement.

To achieve your retirement goals, it's therefore critical to earn a good return on your money while you're retired, not just while you're making contributions. In early retirement, most money you withdraw comes from your investment returns, only later do you start drawing down on your capital.

So, even if your super balance has dropped in recent months, it's not all bad news. There's still plenty of time for your investment to continue to grow while you enjoy life as a retiree.

## 2. Invest wisely

Having the right mix of assets is essential during your working life and when you retire. The 10/30/60 rule clearly shows why.

Many people mistakenly think once they retire their money stops growing. But a sound long-term investment strategy should keep your nest egg growing as you start to withdraw from it, based on your investment timeframe and tolerance for risk.

Including growth assets (shares and property) potentially allows you to generate higher investment returns and therefore prolong the need to draw down on your capital. Plus, being too cautious might mean your money doesn't

generate enough growth and your retirement savings may not last throughout your lifetime. Ensuring your super is well-diversified can help smooth out and reduce the volatility of returns and severity of any negative periods.

## 3. Be market aware

No-one knows how share markets will behave in the future. After all, who could have foreseen the COVID-19 pandemic – a health crisis with such devastating economic consequences.

However, history shows us markets are cyclical and after a fall comes a rise. The challenge for pre-retirees is how to manage an unexpected market downturn close to their retirement date.

Having an eye on financial markets as well as a good relationship with a financial adviser can provide reassurance during difficult times. Investors who panic and cash out their investments after share markets have fallen often regret their decision, having both crystallised their losses and potentially missing out on any upside when markets recover. But that doesn't mean you shouldn't adapt to changes in market conditions as you approach retirement, regardless of whether markets are booming or declining.

## 4. Consider a transition to retirement strategy

If you're asking yourself, "when can I retire?", you could consider a transition to retirement (TTR) strategy. If you've reached your preservation age and you're still working, it could be an effective way to reduce your working hours without reducing your income<sup>2</sup>.

Work fewer hours and use a TTR pension to supplement your income.

Salary sacrifice some of your salary into super and use a TTR pension to replace the lost income, even if you continue working full-time.

The taxation benefits of TTR is one of the big drawcards.

If you're aged over 60, any money you receive from a TTR pension is completely tax free.

And even for those under 60, when you salary sacrifice or make a voluntary concessional contribution into your super, these are taxed at the concessional rate of 15%. Plus, all earnings are also taxed at 15%, rather than your marginal rate, which is generally better than investment earnings outside super.

The other advantage of TTR is the ability to use the income to pay off non-deductible debt like a home loan or credit cards. This could reduce your overall financial burden or even remove completely it by the time you retire.

## 5. Take your time

If you're thinking about retiring this year, make sure you've given yourself time to plan properly – and that includes planning for the unexpected.

The Government has given retirees a helping hand during the current pandemic and reduced the minimum pension drawdown rates for retirees. This means they aren't forced to sell their assets at a time when their value is reduced just to fund their income stream.

But this is unlikely to be the case in every market downturn.

A major risk facing all pre-retirees is sequencing risk – the risk that the timing of withdrawals from super will damage your overall return because financial markets fall all in the years leading up to your retirement<sup>3</sup>. You may choose to delay retiring, reduce your spending, postpone travel plans or make different lifestyle choices.

Good financial habits hold true in retirement as well as when you're working. So, think about how your living expenses will change when you retire and make sure you have enough accessible cash to cover a couple of years ahead. It's the same as having emergency funds while you're working to cover daily essentials and means if financial markets drop again or continue to be volatile, you won't have to sell shares or bonds at a low price.

## Keep the dream of retiring this year

There's no one right answer to the question "when can I retire?". Your circumstances will let you know when the time is right for you.

Financial markets will always be unpredictable so have a plan you're comfortable with and follow it. Invest according to your risk tolerance and find the appropriate balance between short-term accessible cash and long-term investment growth so you can enjoy a long and happy retirement.



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