MONEY MATTERS.

Advice. Life. Investments. Superannuation and Retirement.

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Three reasons not to be afraid of retirement

Why life insurance is still a good deal

How the pandemic changed the equity market

Is buying a home the best investment you'll ever make?

Equity markets hit record highs as optimism surges

Three reasons to not be afraid of retirement

Retirement marks a new beginning but many retirees lack the confidence to enjoy it.

Many older Australians worry they will outlive their retirement nest egg but a recent government report suggests those worries might be misplaced.

The Retirement Income Review **(RIR)** found most retirees leave the bulk of the wealth they had at retirement as a bequest[1].

"The system is designed on the basis that people should draw down their savings to support them in retirement," the RIR found[1].

Yet they don't. Instead, many live off the returns from their retirement savings rather than draw down the capital.

Super is an important pillar that supports retirees' lifestyles – but it's not the only thing holding it up. A closer look at the facts can give retirees the confidence they need to enjoy retirement.

The family home can provide a source of income

The home can be a gold mine if you know where to dig. Older Australians hold a combined half a trillion dollars of value in their homes, according to a 2018 ASIC report.

Yet most people leave its value untapped, with many viewing the home as sacrosanct.

The RIR suggested older Australians would enjoy a higher standard of living by tapping into this value. There are new ways to do this that don't involve selling the home.

The government's Pension Loans Scheme **(PLS)** – its version of a reverse mortgage product – is one option.

The PLS allows retirees to draw down a tax-free fortnightly income stream, with the possibility of lump sums being available from 1 July 2022, from their home equity.

The scheme was made even more attractive in this year's Federal Budget. A 'no negative equity guarantee' eliminates the risk that borrowers may end up repaying more than the market value of their property.

"Using relatively small portions of home equity through the Pension Loans Scheme or similar equity release products can substantially improve retirement incomes for many people," the RIR said.

Another feature of this year's budget is the proposal to extend Downsizer contributions from 1 July 2022, to people aged over 60, down from 65 previously. Up to $300,000 from the sale can be made as a special super contribution.

The Age Pension acts as an investment buffer

Millions of Australians receive the government Age Pension, which ensures the retirement system is equitable.

If markets fall and the value of a retirees' investments decline, the Age Pension automatically picks up some of the slack because it is means-tested. Even most relatively wealthy Australians will be eligible for a part Age Pension as they draw down on their super over time.

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We hope you enjoy our latest edition of Money Matters.

Please contact our office if you would like to discuss anything in this edition.

Greg Roberts

Damien Roberts

Actuarial firm Milliman modelled thousands of future scenarios for retired couples, demonstrating that the potential future Age Pension payments they might receive over the next 25 years have a median value of around $180,000[2].

“The government Age Pension can potentially offset a one-third decline in the value of a wealthy retired couple’s investment portfolio,” according to the Milliman analysis.

This buffer should provide retirees with comfort in the face of uncertainty, such as the COVID-19 pandemic or the Global Financial Crisis, which wiped billions of dollars from super funds.

Most adult children can look after themselves

Some may frown on ‘spending the kid’s inheritance’ but they shouldn’t – at least when it comes to super.

With the average Australian living to about 82 years of age, an inheritance will end up in the hands of children who are likely in their pre-retirement years themselves.

Even the then Treasurer and now Prime Minister, Scott Morrison, in 2015 said retirees shouldn’t use their super as a tax-advantaged inheritance vehicle.

“The purpose of providing tax incentives to encourage people to build up their super is so they can draw down on it in their retirement, not maintain it as a capital pool to be passed on as an inheritance,” he said[3].

Most adult children are functioning members of society and can support themselves.

The RIR also found this process of fostering intergenerational wealth exacerbates the wealth divide for future Australians.

“Most people die with the majority of wealth they had when they retired. If this does not change, as the superannuation system matures, superannuation balances will be larger when people die, as will inheritances.”

If you would like to review your current or projected levels of retirement income, contact your adviser.

1 Retirement Income Review - Final Report | Treasury.gov.au. (2021, May 27). Retrieved from https://treasury.gov.au/publication/p2020-100554

2 Why the Age Pension helps retirees with losses in turbulent times. (2020, April 02). Retrieved from https://au.milliman.com/en/insight/Why-the-Age-Pension-helps-retirees-with-losses-in-turbulent-times

3 Tingle, L. (2015). Scott Morrison tells retirees they must spend their superannuation. Australian Financial Review. Retrieved from https://www.afr.com/wealth/superannuation/scott-morrison-tells-retirees-they-must-spend-their-superannuation-20150524-gh8gz2

Why life insurance is still a good deal

New data shows life insurance provides immense value, yet many Australians are turning their back on this crucial safety net. A government review may be about to change the situation.

New industry statistics show that life insurance remains one of the best value safety nets consumers can buy – yet many people remain underinsured.

The industry approved 96.4% of life cover claims on average and took just 1.5 months to pay last year when a financial adviser was involved, according to data from the regulator[1].

Advisers, who can help navigate the claims process, are playing a key role with just 90% of claims approved when a policy is sold directly through an insurer. The worst insurer selling direct to the public approved only 83.1% of claims.

Yet despite this data showing life insurers are quick, efficient and approve most claims, fewer people are buying insurance.

The total sum insured decreased by 17% and 19% for death and total permanent disability **(TPD)** cover respectively since June 2018, according to a separate analysis of APRA data by actuarial firm Rice Warner[2].

The government tick of approval

Sales have been partially hurt by new regulations affecting superannuation and financial advisers, yet the government has shown its support for the industry and the benefits it provides. The Minister for Superannuation, Financial Services and the Digital Economy, Jane Hume, told an industry gathering in April the story of a small business owner in his 40s who was struck down with cancer[3].

"He stepped away from the business, but he still had bills to pay and a family to provide for. So, he made a claim on his trauma insurance. The insurance meant he was able to keep his business afloat and keep his family living comfortably."

The government has now tasked Treasury to review how current regulatory settings are working and whether they are helping deliver quality financial advice and adequate life insurance to the community.

"When hardworking Australians take out life insurance products, they take personal responsibility for the wellbeing of their dependents. Working Australians are wise to save for a rainy day – they are even wiser to take out insurance."

While the drop in recent life insurance sales has been across all channels – advised, non-advised or through super – getting financial advice ensures cover meets your unique needs.

"It therefore goes without saying that consumers should, wherever possible, have access to high-quality advice when making these decisions," she said. "Advisers will play an increasingly important professional role in the lives of Australians."

Yet, only 20% of Australians are insured through an adviser, according to Hume[3].

Treasury set to review life insurance reforms

While most people have life insurance attached to their super funds, sales of individual life insurance policies may have been affected by recent commission cuts.

Commissions, which help subsidise the cost of advice, were reduced in 2018 through the Life Insurance Framework (LIF). Hume says commissions are only a problem when they influence the advice provided.

"I recognise that a flat fee charged for advice can be a challenging business proposition. Consumers struggle to understand what they are paying for. They may not have the cash to pay upfront themselves," Hume said.

"In short, the problem is when an adviser receives conflicted remuneration."

Treasury will next year review the impact of commission cuts and how they have affected advice. It will also look at a range of other recent regulation to ensure Australians have better access to advice.

How to check whether your life insurer is value for money

The corporate regulator recently launched a new portal that allows Australians to compare the claims and payout times of life insurance products sold through different channels.

ASIC's MoneySmart Life Insurance site explains the different types of life insurance cover and ensures Australians know what to look for before purchasing cover.

The key feature is its life insurance comparison tool, which allows people to compare the percentage of claims a life insurance company pays out, how long an insurance company takes to pay a claim, and the number of disputes consumers have lodged about claims with an insurer.

The website can be accessed at: **https://moneysmart.gov.au/how-life-insurance-works.**

To review your life insurance cover, contact our office today.

1 Life insurance claims comparison tool - Moneysmart.gov.au. (2021, May 21). Retrieved from https://moneysmart.gov.au/how-life-insurance-works/life-insurance-claims-comparison-tool

2 New research shows a larger underinsurance gap - Rice Warner. (2021, April 27). Retrieved from https://www.ricewarner.com/new-research-shows-a-larger-underinsurance-gap

3 Address to the 12th Annual Financial Services Council's Life Insurance Summit 2021 | Treasury Ministers. (2021, May 21). Retrieved from https://ministers.treasury.gov.au/ministers/jane-hume-2020/speeches/address-12th-annual-financial-services-councils-life-insurance

How the pandemic changed the equity market

A market crash reshapes economies and markets. The impact of the recent pandemic is still playing out in new and unexpected ways.

The COVID-19 pandemic created winners and losers on the share market. While some sectors are still struggling to recover and face significant uncertainty, others are surging.

But today's winner is often tomorrow's loser.

A look back at 2020's dramatic market drop provides some timely lessons about the benefits of diversification that can ultimately help protect investor portfolios against the next shock.

What was hot: materials

After spending years recovering from the end of the last mining boom, the S&P/ASX 200 Materials index finally hit new heights. Aussie giants Rio Tinto and BHP grew by more than 30% year-on-year to May.

A key reason was surging demand from China for Australian iron ore, which pushed the commodity's price higher. Meanwhile, iron ore exports from Brazil – the second-largest iron ore exporter to China behind Australia – slowed as it grappled with debilitating COVID-19 outbreaks.

Government incentives such as HomeBuilder also contributed to a property boom, which has also helped drive up the sector.

What was not: utilities and energy

With the economy locked down for long periods during COVID-19 outbreaks and wider macro-economic forces at play, demand for energy dramatically slowed. ASX energy shares dropped by more than 27% in 2020.

And while the sector has recovered from a sharp plunge in oil prices, by May 2021 it was still down by around one-third compared to February last year.

Australia's utility companies suffered a similar fate. Demand for water, electricity and gas slowed and the sector dropped 16.1% last year. Shares in Australian utility giants Origin Energy and AGL dropped to their lowest levels since 2004.

What was on fire: technology

Global giants Amazon, Netflix and Zoom all experienced breakout years as stay-at-home orders and snap lockdowns forced people to switch physical activities such as shopping, entertainment, and work to the virtual world.

The Aussie information technology sector grew 57.8% last year, following the US tech-heavy NASDAQ index, which more than doubled within a year.

ASX market darlings such as Afterpay and Xero reached new heights, with the stocks ending the year 1119% and 146% respectively higher than their March lows.

More recently, the surging sector may have become overvalued, prompting a tech sector selloff early in 2021.

What was not, then hot again: consumer discretionary and financials

Consumer discretionary spending fell into a deep hole in the middle of 2020 as the recession took hold.

Unemployment soared and spending plummeted as shops, transport, and events were shut down.

People increased their savings until JobSeeker payments were doubled and JobKeeper business payments pumped up the economy.

The sector finished 2020 with an 11.3% gain, bouncing back from a 45% fall between March and April.

Similarly, the financial sector struggled amid concerns there would be mass defaults on mortgages and business loans. The sector finished 6.6% down for the year but has since grown by 17% in the first five months of 2021 as the economy rebounded and property prices boomed.

Diversification: preparing your portfolio for the unforeseeable

COVID-19 fundamentally changed almost every market in the world. But the performance of each sector was partly down to luck, given no one predicted a global pandemic or Australia's faster-than-expected recovery.

This is why diversification should be a core strategy for all investors. It spreads out investment risk and ensures that all the eggs in your basket don't break at once.

Holding one or two stocks – even blue-chips such as the big banks – increases investment risk. Even banks made rare cuts to their dividends as COVID-19 struck.

A more diversified portfolio could include dozens (or hundreds) of stocks diversified across sectors and geographies. Even more diversification can be obtained by adding different asset classes such as bonds, property, and less-common classes such as infrastructure.

A portfolio should also include easy-to-access sources of income such as cash, so you're never forced to sell shares when a downturn strikes.

If you'd like to review your investment portfolio, please contact our office to schedule an appointment with your adviser.

Is buying a home the best investment you'll ever make?

House prices are soaring, but investors rarely consider the hidden costs and the benefits of a more diversified investment strategy.

If you've been to a property auction lately, you'd be forgiven for thinking you were somewhere on Wall Street during the booming 1980s.

Frenzied flocks of potential buyers shift nervously and eyeball potential rivals. A combination of manic phone calls and panicked whispers flow through the crowd, driven by a market boom and that all-too-familiar FOMO feeling.

It's cutthroat out there – and no wonder. CoreLogic's monthly home value index rose 2.8 per cent in March — the biggest monthly growth since October 1988[1]. But are these dizzying returns all they're cracked up to be?

Over the longer-term, national housing prices rose by 412 per cent between 1993 and 2018, according to CoreLogic[2]. In comparison, the ASX All Ordinaries index (a broad indication of the Australian stock market) had risen by just 261 per cent.

Don't forget transaction costs

However, most property investors forget about the buying and selling costs involved in property.

It costs thousands of dollars for conveyancing fees, building and pest inspections, mortgage application fees, as well as transfer and registration fees. Mortgage insurance, which protects the lender if the borrower defaults on the loan, is mandatory if the borrower has less than a 20 per cent deposit.

But stamp duty is invariably the major cost. While most States offer some stamp duty exemptions or concessions for first home buyers and others, most people must pay the full tax.

The median NSW house price of about $1.3 million currently attracts stamp duty of approximately $60,000, according to a Domain housing report[3].

Don't forget the hidden cost of maintenance and renovations

Properties don't maintain themselves – property owners quickly become acquainted with electricians, plumbers and a host of other tradies that can charge big bucks.

Renovations also don't come cheap.

The median spend for home renovation projects was $20,000 in 2019, but 10% of homeowners spent $150,000 or more, a report by Houzz and Home Australia found[4].

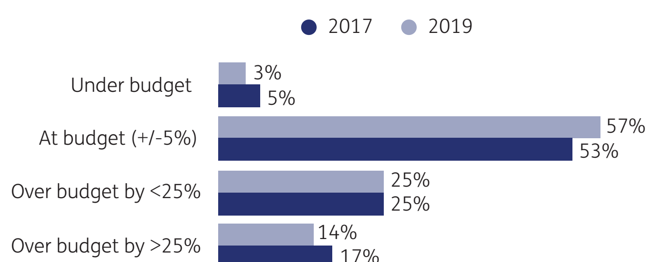
Roy Morgan Research CEO Michele Levine says homeowners typically renovate within a year of buying.

"This suggests that they have recently purchased and moved into a home previously owned by someone else and are making their own mark on it," Levine said while presenting the findings[5].

Roy Morgan Research found that 8.4 million (or 62%) of Australia's 13.6 million homeowners undertook renovations in 2016 – up from 7.5 million three years earlier. More recently, the government's HomeBuilder grant has helped re-ignite a renovation boom.

While renovating your house can improve its value, it can also leave a serious dent in your returns. The Roy Morgan report also found 39 per cent of renovations ran over budget.

Frequency of renovation budgets among homeowners who renovated in 2017 vs. 2019



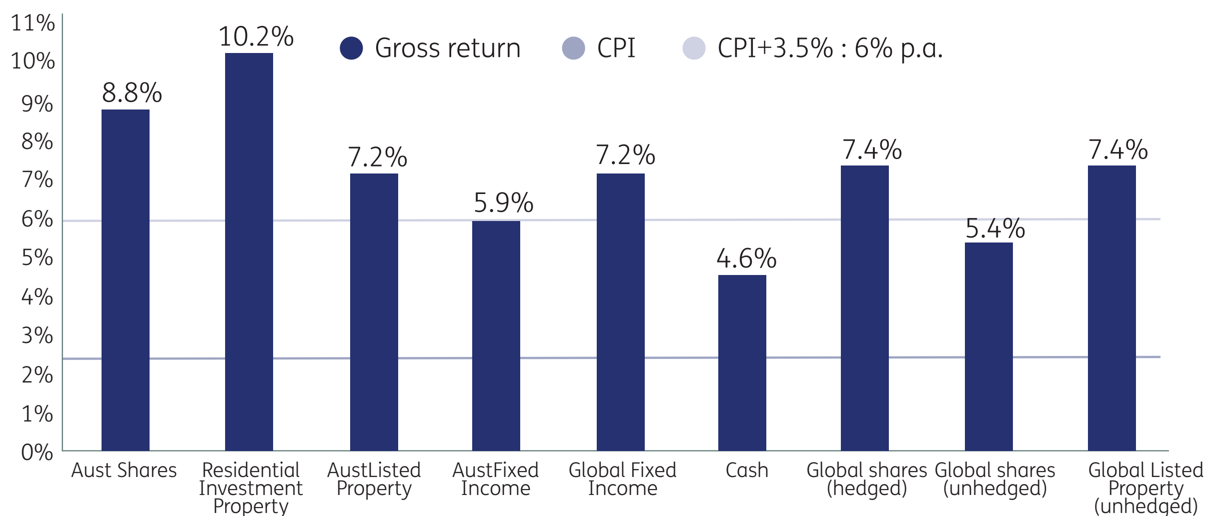
Source: Renovation Nation: home improvement in Australia – Roy Morgan Research.

Think about diversifying, and don't forget shares

Most people forget how long they own property – they only look at the initial price they paid and the final sale price. They rarely include costs and work out the true annual return, which would make a fairer comparison with the share market.

An analysis of Australian residential property returns by the ASX and Russell Investments in 2018 found it was the best performing asset class over the long-term[6]. However, it was also the worst performer (below cash and Australian bonds) in 2004 and 2005.

Comparison across asset classes on a before tax basis: 20 years to December 2017



Note: All returns are gross of tax and costs. Past performance is not a reliable indicator of future performance

Source: 2018 Russell Investments/ASX Long Term Investing Report

There's money to be made in both property and stocks. Australia has had a solid run in both asset classes for many years.

However, investors should consider diversifying their investments rather than overloading on property, no matter how much the market may be booming in the short-term.

If you have any concerns about property, stocks or your portfolio's diversification, contact our office today and speak with your adviser.

1 National home value index rises at its fastest pace in 32 years. (2021, June 02). Retrieved from https://www.corelogic.com.au/news/national-home-value-index-rises-its-fastest-pace-32-years

2 25 years of housing trends | Go straight to Aussie. (2021, May 13) Retrieved from https://www.aussie.com.au/plan-compare/property-reports/25-years-of-housing-trends-property-market-report.html

3 Razaghi, T. (2021). Sydney house prices soar to record median of $1.3m after fastest quarterly rise in 28 years. Domain. Retrieved from https://www.domain.com.au/news/sydney-house-prices-soar-to-record-median-of-1309195-after-fastest-quarterly-rise-in-28-years-1048412

4 2020 AU Houzz & Home Renovation Trends Study. . . Retrieved from https://www.houzz.com.au/magazine/2020-au-houzz-and-home-renovation-trends-study-stsetivw-vs~135007238

5 Renovation Nation: home improvement in Australia. (2021, June 02). Retrieved from https://www.roymorgan.comfindings/7102-renovation-nation-home-improvement-in-australia-201701090848

6 2018 Russell Investments/ASX Long Term Investing Report. Retrieved from https://www.asx.com.au/documents/research/russell-asx-long-term-investing-report-2018.pdf

Equity markets hit record highs as optimisim surges

Investment markets continued to surge despite ongoing concerns about long-term inflation and the lingering impact of the coronavirus pandemic.

The US and Australian share markets hit record highs in recent months as the global economy continued to rebound from the coronavirus pandemic.

The Australian economy is now stronger than its pre-pandemic levels, despite the hospitality and tourism sectors still struggling amid sporadic lockdowns. Australia's GDP lifted by a strong 1.8% in the March quarter, according to the Australian Bureau of Statistics.

Surging oil and iron ore prices, driven by demand from China, helped power the share market into new territory. Dividend-yielding bank shares rose although utilities continued a gradual decline that started in August last year. While the Australian IT sector suffered from a global tech selloff in the quarter, it remains well up compared to early last year.

The Federal Government's expansionary Budget in May delivered a wide range of business- and consumer-friendly initiatives that have largely been well-received. The big spending Budget is expected to help the economy continue to recover from the pandemic.

Women, taxpayers and small businesses received support, with many pandemic measures extended. Retirees are also set to benefit with $17.7 billion spent on aged care, which includes 80,000 new home care packages over the next two years.

Meanwhile, residential property continues to boom, with all major cities surging thanks to low interest rates and government support programs. A low-interest rate environment is likely to continue for many years, with the RBA announcing it will not increase the cash rate until inflation moves significantly higher.

NAB's April Business Survey found trading, profitability, and employment were all at fresh highs while conditions are likely to remain strong in the near term. Consumer confidence is also positive with the ANZ/Roy Morgan consumer survey finding 38% of families expect to be better off over the next year.

Meanwhile, the US economy is expected to grow by a remarkable 6.3% this year and follow it up with a 4.3% expansion into next year, according to the Philadelphia Fed. Its growth is being spurred by President Biden's US$2.9 trillion stimulus and the success of the country's vaccine rollout.

Potentially higher inflation remains a concern after the US announced higher than expected annual inflation numbers in May.

The pandemic also remains a concern to global economic growth, with outbreaks in India and other regions such as Singapore, creating uncertainty. A slower than expected vaccine rollout in Australia remains a problem, with Victoria plunged into another lockdown in late-May.

Emerging markets such as Brazil, Argentina and India continue to grapple with the brunt of the crisis while developed economies, notably Sweden, the Netherlands and France, are also experiencing serious issues.

Japan's economy has also stagnated over the quarter as it battles a third wave before the Tokyo Olympic Games in July.

However, more than one billion people are now vaccinated, and case numbers are generally declining globally.

If you are concerned about current market conditions, please contact your adviser, who can help at any time.

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