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THE LOOMING INCOME CRISIS

Retirement With the financial pressure growing for many, advisers outline a rethink of income strategies, writes **Duncan Hughes**.

Self-funded retirees in self-managed superannuation funds fear an income crisis because of falling returns, lower dividends and interest rates, and uncertainty over rental returns.

SMSF returns plunged by nearly 10 per cent, or about twice the drop in industry funds, in the three months ended March 31, government statistics show.

"The coming together of falling markets, low-interest rates and economic fallout from COVID-19 is causing an income crisis for retirees," says Wayne Strandquist, president of the Association of Independent Retirees.

"Many self-funded retirees may have assets but they cannot get sufficient return to generate an income to live," Strandquist says.

"Most are relying on their reserves of cash. But the financial pressure is growing more desperate the longer it goes on."

Alex Dunnin, director of research for Rainmaker Information, which monitors the performance of super funds, blames the underperformance of SMSFs in the first quarter on their high exposure to Australian equities.

That period covers the initial slump in the stock market as global markets reacted to the economic and financial impact of COVID-19.

Between February 21 and March 23, the S&P/ASX 200 Index plunged nearly 45 per cent to 4546 points. It has since recovered and was this week trading around 5800.

Brendan Ryan, principal of Later Life Advice, an independent financial adviser, says it is time for SMSF members and other self-funded retirees "to pause and rethink".

"It is pure luxury [for the majority of retirees] to think they can live on investment income," he says.

"Now is the time to take a laser-like look at the mix of retirement assets," Ryan adds.

That includes looking at the mix of investment income, some government support and possibly drawing down capital from assets, such as considering a reverse mortgage.

The equity in the family home for an estimated 4.5 million retirees is on average worth four to five times as much as their superannuation savings, which for male Baby Boomers equal about $150,000 and for females about $80,000, according to Household Capital, which specialises in the products.

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> Brendan Ryan, Later Life Advice

Paul Moran, principal of Moran Partners Financial Planning, suggests avoiding investment risks and deferring significant costs, such as overseas travel or renovations. He adds: "Super strategies need to robust. There are times to grow returns and periods to preserve capital. This is a time to preserve capital."

Other options include considering semi-retirement, which might involve working a few days a week, or months a year, to supplement income.

"That way you can use super to top up your reduced work income," Moran says.

"Two or three years of negative returns and volatility will impact your funds in the short term. But if you preserve as much capital as possible you'll get the benefit when market strength returns."

According to long-standing estimates from the Association of Superannuation Funds of Australia, the average super balance required to achieve a comfortable retirement is $640,000 for couples and $545,000 for singles (assuming they withdrew super as a lump sum and received a part-age pension).

'This is a time to preserve capital,' says Paul Moran of Moran Partners Financial Planning.

A comfortable retirement includes having access to a range of recreational activities, paying top-level private health insurance, owning a mid-range car and occasional travel.

Strandquist says these lump sums could have provided a comfortable lifestyle five years ago when bank term deposits paid about 5 per cent, franked dividend income from blue-chip bank stocks was about 7 per cent and residential and small commercial real estate investment returns were comfortably above inflation.

But blue-chip companies have deferred or slashed dividends, term deposits continue to fall and rental property income has been hit by new government rules that encourage rents to be renegotiated if tenants are stood down from work.

Banks continue to chip away at deposit rates. For example, CBA has reduced its eight-month term deposit by 10 basis points to 1 per cent, according to Canstar, which monitors rates and fees. Rates on more than 300 term deposits were cut in May, with average decreases ranging from 13 to 26 basis points.

Global investment bank Morgan Stanley is warning property investors to expect a "rental-led downturn".

House prices fell 0.5 per cent in May, the first fall in a year. "We expect softness to continue, with turnover and rents more significantly impacted," the bank warns.

Specialist fixed income fund managers, such as Cameron Harrison, warn that cash rates, currently at 0.25 per cent, could take many years to start increasing.

According to the SMSF Association, there are about 560,000 self-managed super schemes and more than 1 million members. More than one in three members, or more than 400,000 individuals, are of retirement age, according to the Australian Taxation Office.

Overall, the nation's $2.9 trillion pool of super savings has weathered the worst of COVID-19's financial impact "remarkably well", falling just 0.3 per cent in the 12 months to the end of March, says Rainmaker's Dunnin. SI

How success can ruin portfolios

Strategy

Michael McCarthy

Managing financial market traders is challenging. The very qualities that make them good traders, such as independent thinking and high self-confidence, can make them hard to direct.

Issuing orders to them can, therefore, be counter-productive, and many managers use a light touch. But there are two moments when traders are most in economic danger and require close supervision.

The first is obvious. Any time a trader suffers a large loss, they are in danger. Some lose their confidence while others become reckless. Neither is likely to lead to success in the markets.

The other time of high danger is less intuitive. Traders are also a threat to the bottom line after a big win, as it can erode their appreciation of risk.

This second threat has meaning for investors, especially those who are newer to the sharemarket. The 34 per cent jump in the S&P/ASX 200 Index from the lows of March to last week took many professional investors by surprise. By contrast, Australian stockbrokers with mainly individual investors as clients saw net buying through March and April. In most cases, those buyers are sitting on substantial gains.

They're not hard to find. In chat rooms and in tweets, there is a lot of "I told you so" going around.

Perhaps the most mentioned stock is Afterpay Touch (APT). Initially, the retail payments provider fell harder than the broader market, dropping from higher than $40 to touch $8. The resurgence since the March low is even more spectacular, taking APT to an all-time high just above $50.

> *Problems arise when investors start to think of themselves as 10 feet tall and bulletproof.*

This means anyone who bought as APT fell, or jumped in on the way up, is in profit. Those who bought near the low are looking at a "six-bagger", or six times their initial investment, and any traders using leveraged instruments like contracts for difference may have picked up even better returns on capital. All of them have good reason to be pleased.

However, this is where the danger starts. Large profits can induce overconfidence not only in hardened traders but in less experienced investors. Further, investors who have done well over the last two months did so despite many professional investors and analysts warning that the economic damage from containment measures made sharemarkets vulnerable to further selling.

Healthy scepticism about "experts" is useful, but problems arise when investors start to think of themselves as "10 feet tall and bulletproof".

The threat from overconfidence can lead to ignoring warning signs. Nobody knows the future, and when investors stick with losing positions due to a misplaced trust in their judgment, they can do much damage to their portfolios.

The reality is there are still conflicting currents affecting the global outlook. Easing lockdown measures are clearly positive. So, too, is the fact the US President talked tough on Hong Kong but did not detail any specific action. This takes some of the heat out of the recent disputes between China and the US.

Against this good news is the possibility that both of these positives could reverse. Secondary viral outbreaks are a concern, as is the looming US election and the potential for new Sino-US disputes for domestic political purposes.

The evidence of macro-economic damage and the hit to many companies' bottom lines are further reasons for investor caution. This is offset somewhat by central bank and government action, but the overall outlook for growth over the next year is sombre.

These opposing economic forces mean that market sentiment can swing sharply. At the moment sentiment is very positive, possibly at peak positive. The right decision for any investor depends on individual circumstances, as well as the market. Investors sitting on substantial gains could consider taking some profit, or at least taking a break, to allow the emotional tide spurred by solid wins to recede.

Hubris is the number one killer of trading careers and it can be similarly dangerous to investing success. SI

Michael McCarthy is chief market strategist at CMC Markets.

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