MONEYNEWS
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Investing Lessons From The Pandemic

When the coronavirus pandemic hit financial markets in March 2020, almost 40 per cent was wiped off the value of shares in less than a month.[i] Understandably, many investors hit the panic button and switched to cash or withdrew savings from superannuation.

With the benefit of hindsight, some people may be regretting acting in haste. Although for others, accessing their super under the early release due to COVID measures was a difficult but necessary decision at the time.

As it happened, shares rebounded faster than anyone dared predict. Australian shares rose 28 per cent in the year to June 2020 while global shares rose 37 per cent. Balanced growth super funds returned 18 per cent for the year, their best performance in 24 years.[ii]

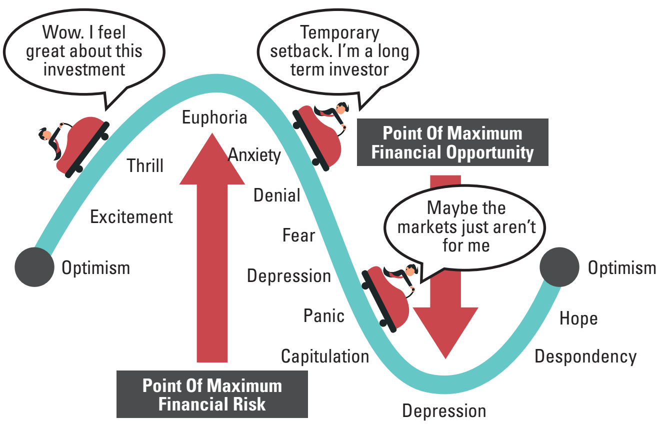
While every financial crisis is different, some investment rules are timeless. So, what are the lessons of the last 18 months?

Lesson #1 Ignore the noise

When markets suffer a major fall as they did last year, the sound can be deafening. From headlines screaming bloodbath, to friends comparing the fall in their super account balance and their dashed retirement hopes.

Yet as we have seen, markets and market sentiment can swing quickly. That's because on any given day markets don't just reflect economic fundamentals but the collective mood swings of all the buyers and sellers. In the long run though, the underlying value of investments generally outweighs short-term price fluctuations.

One of the key lessons of the past 18 months is that ignoring the noisy doomsayers and focussing on long-term investing is better for your wealth.



Lesson #2 Stay diversified

Another lesson is the importance of diversification. By spreading your money across and within asset classes you can minimise the risk of one bad investment or short-term fall in one asset class wiping out your savings.

Diversification also helps smooth out your returns in the long run. For example, in the year to June 2020, Australian shares and listed property fell sharply, but positive returns from bonds and cash acted as a buffer reducing the overall loss of balanced growth super funds to 0.5%.

The following 12 months to June 2021 shares and property bounced back strongly, taking returns of balanced growth super funds to 18 per cent. But investors who switched to cash at the depths of the market despair in March last year would have gone backwards after fees and tax.

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The New Financial Year Rings In Super Changes

As the new financial year gets underway, there are some big changes to superannuation that could add up to a welcome lift in your retirement savings.

Some, like the rise in the Superannuation Guarantee (SG), will happen automatically so you won't need to lift a finger. Others, like higher contribution caps, may require some planning to get the full benefit.

Whether you are just starting your super journey or close to retirement, a member of a big super fund or your own self-managed super fund (SMSF), it pays to know what's on offer.

Here's a summary of the changes starting from 1 July 2021.

Increase in the Super Guarantee

If you are an employee, the amount your employer contributes to your super fund has just increased to 10 per cent of your pre-tax ordinary time earnings, up from 9.5 per cent. For higher income earners, employers are not required to pay the SG on amounts you earn above $58,920 per quarter (up from $57,090 in 2020-21).

Say you earn $100,000 a year before tax. In the 2021-22 financial year your employer is required to contribute $10,000 into your super account, up from $9,500 last financial year. For younger members especially, that could add up to a substantial increase in your retirement savings once time and compound earnings weave their magic.

The SG rate is scheduled to rise again to 10.5 per cent on 1 July 2022 and gradually increase until it reaches 12% on 1 July 2025.

Higher contributions caps

The annual limits on the amount you can contribute to super have also been lifted, for the first time in four years.

The concessional (before tax) contributions cap has increased from $25,000 a year to $27,500. These contributions include SG payments from your employer as well as any salary sacrifice arrangements you have in place and personal contributions you claim a tax deduction for.

At the same time, the cap on non-concessional (after tax) contributions has gone up from $100,000 to $110,000. This means the amount you can contribute under a bring-forward arrangement has also increased, provided you are eligible.

Under the bring-forward rule, you can put up to three years' non-concessional contributions into your super in a single financial year. So this year, if eligible, you could potentially contribute up to $330,000 this way (3 x $110,000), up from $300,000 previously. This is a useful strategy if you receive a windfall and want to use some of it to boost your retirement savings.

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More importantly, over the past 10 years balanced growth funds have returned 8.6 per cent per year on average after tax and investment fees. High growth funds returned 10.3 per cent per year and the most conservative funds returned 5.5 per cent per year.[ii]

The mix of investments you choose will depend on your age and tolerance for risk. The younger you are, the more you can afford to have in more aggressive assets that carry a higher level of risk, such as shares and property to grow your wealth over the long term. But even retirees can benefit from having some of their savings in growth assets to help replenish their nest egg even as they withdraw income.

Lesson #3 Stay the course

The Holy Grail of investing is to buy at the bottom of the market and sell when it peaks. If only it were that easy. Even the most experienced fund managers acknowledge that investors with a balanced portfolio should expect a negative return one year in every five or so.

Unfortunately, we can only ever be sure when a market has peaked or troughed after the event, by which time it's usually too late. By switching out of shares and into cash after the market crashed in March last year, investors would have turned short-term paper losses into a real loss with the potential to put a big dent in their long-term savings.

Even if you had seen the writing on the wall in February 2020 and switched to cash, it's unlikely you would have switched back into shares in time to catch the full benefit of the upswing that followed.

Timing the market on the way in and the way out is extremely difficult, if not impossible.

Looking ahead

Every new generation of investors has a pivotal experience where lessons are learned. For older investors, it may have been the crash of '87, the tech wreck of the early 2000s or the global financial crisis. For younger investors and many older ones too, the coronavirus pandemic will be a defining moment in their investing journey.

Now that shares and residential property prices have rebounded strongly, investors face new challenges. That is, how to make the most of the prevailing market conditions while ignoring the FOMO (fear of missing out) crowd.

By choosing an asset allocation that aligns with your age and risk tolerance then staying the course, you can sail through the market highs and lows with your sights firmly set on your investment horizon. Of course, that doesn't mean you shouldn't make adjustments or take advantage of opportunities along the way.

We're here to guide you through the highs and lows of investing, so give us a call if you would like to discuss your investment strategy.

i https://www.forbes.com/sites/lizfrazierpeck/2021/02/11/the-coronavirus-crash-of-2020-and-the-investing-lesson-it-taught-us/?sh=241a03a46cfc

ii https://www.chantwest.com.au/resources/super-funds-post-a-stunning-gain

More generous Total Super Balance and Transfer Balance Cap

Super remains the most tax-efficient savings vehicle in the land, but there are limits to how much you can squirrel away in super for your retirement. These limits, however, have just become a little more generous.

The Total Super Balance (TSB) threshold which determines whether you can make non-concessional (after-tax) contributions in a financial year is assessed at 30 June of the previous financial year. The TSB at which no non-concessional contributions can be made this financial year will increase to $1.7 million from $1.6 million.

Just to confuse matters, the same limit applies to the amount you can transfer from your accumulation account into a retirement phase super pension. This is known as the Transfer Balance Cap (TBC), and it has also just increased to $1.7 million from $1.6 million.

If you retired and started a super pension before July 1 this year, your TBC may be less than $1.7 million and you may not be able to take full advantage of the increased TBC. The rules are complex, so get in touch if you would like to discuss your situation.

Reduction in minimum pension drawdowns extended

In response to record low interest rates and volatile investment markets, the government has extended the temporary 50 per cent reduction in minimum pension drawdowns until 30 June 2022.

Retirees with certain super pensions and annuities are required to withdraw a minimum percentage of their account balance each year. Due to the impact of the pandemic on retiree finances, the minimum withdrawal amounts were also halved for the 2019-20 and 2020-21 financial years.

Age Of Retiree	Temporary Minimum Withdrawal	Normal Minimum Withdrawal
Under 65	2%	4%
65 to 74	2.5%	5%
75 to 79	3%	6%
80 to 84	3.5%	7%
85 to 89	4.5%	9%
90 to 94	5.5%	11%
95 or older	7%	14%

Source: ATO

But wait, there's more

Next financial year is also shaping up as a big one for super, with most of the changes announced in the May Federal Budget expected to start on 1 July 2022.

The Budget included proposals to:

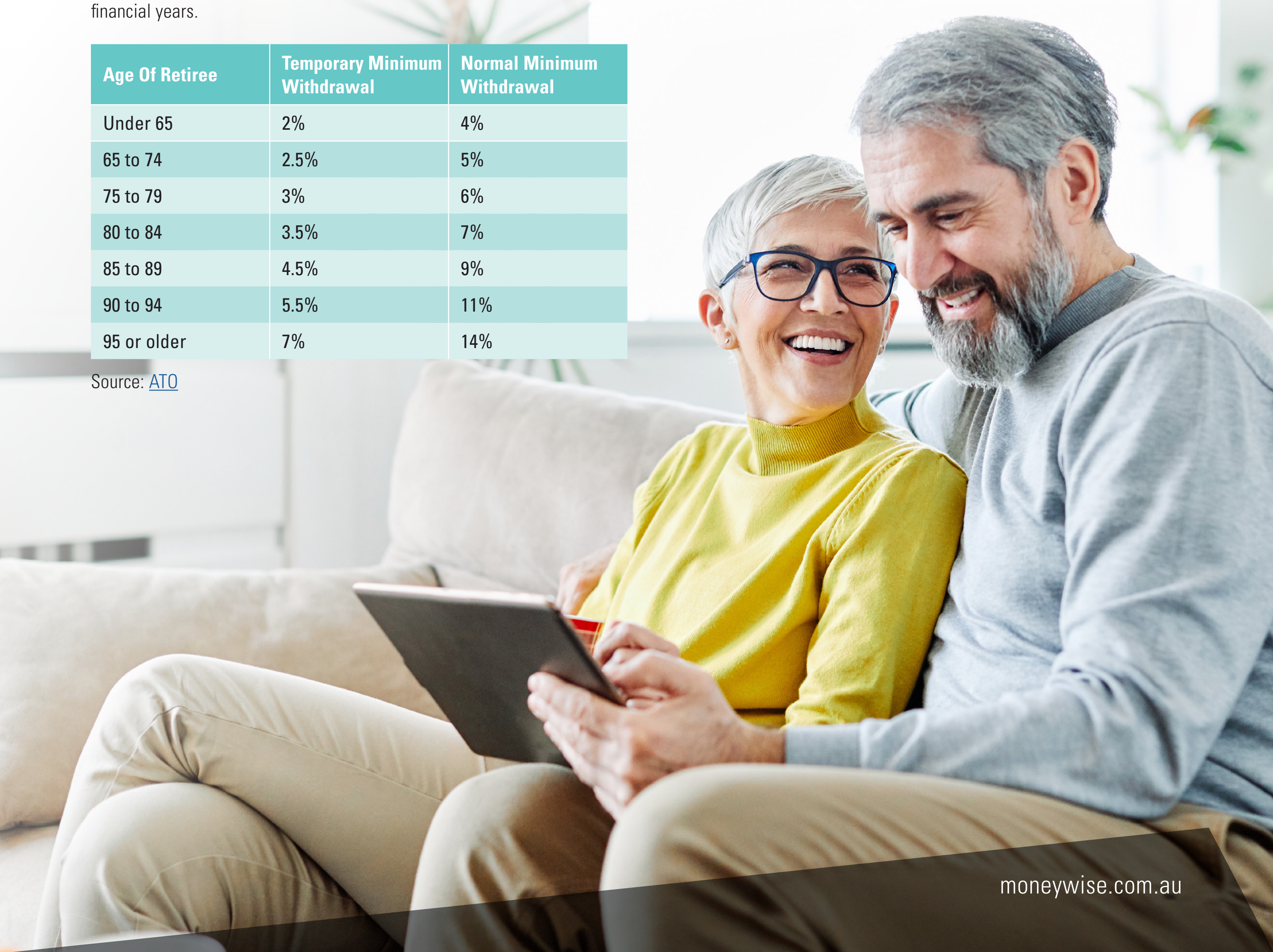
- repeal the work test for people aged 67 to 74 who want to contribute to super
- reduce the minimum age for making a downsizer contribution (using sale proceeds from your family home) from 65 to 60
- abolish the $450 per month income limit for receiving the Super Guarantee
- expand the First Home Super Saver Scheme
- provide a two-year window to commute legacy income streams
- allow lump sum withdrawals from the Pension Loans Scheme
- relax SMSF residency requirements.

All these measures still need to be passed by parliament and legislated.

Time to prepare

There's a lot for super fund members to digest. SMSF trustees in particular will need to ensure they document changes that affect any of the members in their fund. But these latest changes also present retirement planning opportunities.

Whatever your situation, if you would like to discuss how to make the most of the new rules, please get in touch.



Time To Review Your Income Protection Cover

If you've owned an individual income protection or salary continuance policy in recent years, you may have seen your premiums increase as insurers struggled to cover their large losses on these products.[i]

Given the ongoing competition and generous features in some products, the Australian Prudential Regulation Authority (APRA) has decided it's time for some new rules to ensure income protection cover remains sustainable and affordable for customers.

This will result in sweeping changes to these types of policies from 1 October 2021, so it's essential to review your insurance protection cover before insurers start altering their product offerings.

What is income protection?

Income protection cover protects your most valuable asset – your ability to earn an income. It acts as a replacement income if you are injured or disabled and will help support your family and current lifestyle while you recover.

What's more, your premiums are generally tax-deductible, so they can potentially help reduce your tax bill.

Major changes to income protection

Reform of income protection policies started back on 1 April 2020, when insurers were no longer permitted to offer customers Agreed Value income protection policies. Agreed value income protection provided more certainty about the amount you would be paid if you claimed and was based on your best 12 months earnings over a three-year period.

Following this initial change, APRA is implementing further changes from 1 October 2021 that will make new income protection policies much less generous. The reforms mean insurers will be offering new policies that base insurance payments on your annual income at the time you make a claim (or the previous 12 months), not on an agreed earnings amount.[ii]

For people with a fluctuating income, insurance payments will be based on your average annual earnings over a period appropriate for your occupation and will reflect future earnings lost due to the disability.

To further reduce costs, new policies will no longer offer supplementary benefits like specified injury benefits.

Limits on income payments

Other changes include a requirement for the maximum income replacement payment for the first six months to be capped at 90 per cent of earnings, reducing to 70 per cent after six months.[ii] If your insured income amount excludes superannuation, the Superannuation Guarantee can be paid in addition to the 90 per cent cap.

One of the most significant changes is that the terms and conditions of an existing income protection policy will no longer be guaranteed until age 65. Policies will no longer be offered for longer than five years, so your policy and its terms will be reviewed every five years.

You won't need to undergo medical review, but any changes to your occupation, financial circumstances or taking up a dangerous pastime will need to be updated in the policy. Even if your circumstances remain the same, you will still be required to review the policy.

If your policy has a long benefit period, you are also likely to face a tighter definition of disability, rather than the previous definition of simply being unable to perform your 'normal job'. APRA is keen to ensure claimants who are able to return to some form of paid employment do so, rather than remaining at home and receiving a payment.

Impact on existing and new policies

So what does this mean for you?

If you currently have an income protection policy outside your super, you will not be immediately affected by these changes, but it would be wise to check your policy is still appropriate for your circumstances.

Given the extent of the changes to income protection cover, if you have let your insurance lapse or don't currently have income protection, it could make sense to consider signing up before 1 October 2021 to take advantage of the more generous current arrangements.

Income protection is often overlooked because of a perception that it's too costly or not essential, but like all insurance, the cost of not being insured can be far greater. This type of cover offers valuable benefits that should be a key component in your wealth creation – and preservation – strategy.

If you would like help reviewing or selecting appropriate income protection cover, call our office today.

i https://www.apra.gov.au/news-and-publications/apra-resumes-work-to-enhance-sustainability-of-individual-disability-income

ii https://www.apra.gov.au/final-individual-disability-income-insurance-sustainability-measures

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Moneywise Personal Financial Management Pty Ltd

ABN 43 764 170 979
Australian Financial Services Licence 287804
Australian Credit Licence 287804

Level 8, 360 Collins Street,
Melbourne Victoria 3000
PO Box 505 Collins Street West VIC 8007

Telephone: 03 9649 7611
Email: info@moneywise.com.au
www.moneywise.com.au