METROPOLITAN FIRE SERVICE SOUTH AUSTRALIA

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What's inside:

Challenges of ensuring adequate retirement income for Australians

Executive Summary from "The future of retirement income paper" prepared by the Association of Superannuation Funds of Australia (ASFA)

This report is the outcome of collaboration between ASFA and State Street Global Advisors Australia (SSgA). It provides a detailed analysis of the sustainability of Australian retirement savings from the perspective of today's average Australian. Most Australians don't have enough money to retire on. Most recent data (2011/2012) indicates that the average Australian retires with an accumulated balance $197,000 for men and $105,000 for women. It will not be until around 2040 that most Australians will be retiring having contributed to superannuation for their entire working life. As the system matures and the Superannuation Guarantee (SG) contribution is increased to its target level of 12 per cent, accumulation balances at retirement will be larger and the need for retirees to rely, even in part, on the Age Pension will reduce.

The report draws the following conclusions:

1. **The average couple needs just over $500,000 to ensure that they can live comfortably in retirement.** However, this relies on the Age Pension contributing to retiree income and this is only true if the retirees are relatively healthy and own their own home. Critically, while this amount is adequate, it does not factor in the risk of living longer than expected, having to face unexpected health care costs, or changes in the Age Pension arrangements.

2. **That including growth assets in the retirement portfolio, may help to achieve a longer stream of retirement income.** While cash and fixed income investments generate an income stream from interest paid, the growth that is generated from assets like equities and property should result in a retiree's lump sum lasting longer.

3. **Sequencing risk – where money is withdrawn from a superannuation account immediately after the market drops, and before it recovers – is less of a problem in retirement than in the late accumulation stage.** This is because relatively smaller amounts are being withdrawn (and therefore relatively less loss crystallised) compared with the late accumulation phase or at the point of retirement when the asset allocation of the entire portfolio may be shifted dramatically.*

   **The Defined Benefit design of the Scheme enjoyed by Permanent Fire-fighters significantly reduces the pre-retirement risk experienced by Accumulation funds.*

4. **Longevity risk remains a problem for those individuals who outlive their savings.** Without additional protection against the risk of living longer, retirees may see their lifestyle significantly diminished, as they have only the Age Pension to support them when all of their superannuation assets have been spent.

Based on these findings and on other ASFA policy research, we make the following statement:

> *The industry must be able to help retirees by providing retirement products which generate a regular and stable income stream, provide longevity risk management and which are flexible enough to deal with unexpected life events. This will help prevent retirees overspending and running out of income earlier than expected, or conversely under spending and leading an unnecessarily frugal life.*
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> *This means it is vital that the recommendations in relation to the super system by the FSI be implemented, regulatory impediments to income streams product development be removed, the qualifications for financial advisers be reviewed so that increased requirements are placed on those that provide retirement advice and the development of self-guided advice retirement tools be encouraged.*

(continued from page 1)

It will be important not to throw the baby out with the bath water in coming up with the solution to this challenge. Allocated pensions can be appropriate in solving part of the retirement conundrum provided that individual retirees have a disciplined drawdown approach and that the asset allocation is consistent with the projected lifetime. What the industry does need however, are additional products which provide more flexibility and meet the need to protect against the risks of longevity. These may be add-ons to an allocated pension-style product, or a standalone product which bundles together desirable features such as: a regular income stream; a deferred annuity; and a deferred cash lump sum for aged care costs.

While this paper deals with the income which can be generated from portfolios with different mixes of assets, it links closely with the need to help individuals to plan their retirement spending. In the current system, there is no standardised guidance as to how to manage assets in retirement. And this means that decisions which must be made at the point of retirement can be challenging and confusing. As most retirees will not have access to good financial advice, there is a risk that their decision making is sub-optimal, and that they may end up invested in an inappropriate product. Further, ASFA supports the Murray Report recommendations to review the qualifications for financial advisers and to develop self-guided retirement advice tools.

What are you **really worth?**

Unfortunately, there's only one way to know whether you're getting ahead and it involves some simple maths.

It's easy to assume you're doing OK financially if you're driving around in leased car and taking regular holidays in Thailand. But do you ever stop and wonder, as you throw another bank statement in the bin, just what have you got to show for your efforts and what you're actually worth in terms of your wealth?

The only way to know whether you're worth anything (good looks and charitable acts aside) is to calculate your personal net worth. Once you have this number, you can track your financial fortunes over time and see whether you're getting ahead or getting closer to moving back in with your folks.

To calculate your net worth just tally up all your assets (things you own) and subtract your financial liabilities (money you owe). Be realistic about what your assets are worth. A five-year old car may be worth only 60% or even less of what you paid for it. A home theatre system you're buying on hire purchase may be worth half its original value in no time. Include your super in your net wealth – it's not an asset you can cash out now, but it's still one of your larger investments. You can find your current balance by visiting the Scheme's website at **www.samfs.superfacts.com**.

(You'll need your member number and PIN, so call the Helpline on **1300 132 573** if you need your PIN reset or you can reset it online if we have your email address.)

Net worth = What you own – What you owe

The first place to start when counting your assets is the portion you own of your own home (whatever shape that may take, be it a house, unit or townhouse). Basically, it's the value of your property minus the amount you owe on your mortgage if you have one. When estimating the value of your property, research its current market value, which will depend on where you've bought and present demand for similar properties in your area. Remember, what goes up doesn't always stay there.

As we've seen recently in many parts of Australia, property values can go down as well as up. Property in places that have seen crazy increases is particularly vulnerable to price crashes. There are lots of factors that can influence prices; the mining boom being a good example. If you have bought property in an area which has experienced large price increases, be realistic about the value you take into account towards your net worth to avoid an artificially inflated number.

A good case in point is Perth property prices. These boomed by over 40% compared with other Australian capital cities in 2006, only to slump severely and lag behind by almost 10% in late 2008. So be realistic about what your property's worth so you get an accurate picture of your net worth.

When calculating what you owe, factor in all your debts, including HECS, car loans, amounts owed on hire purchase agreements and anything you owe on your credit card that you don't pay off each month. If you own more than you owe, your net worth is positive. If you owe more than you own, you're in debt. If you're paying off a house in Australia, one of the world's most expensive property markets, you may be in debt. That's fine but the idea is that you want to see that debt reduce over time.

And that's what this exercise is really about: tracking your net worth over time to see where it's heading: hopefully in the right direction! At a minimum, do the maths once a year and chart your progress. There are loads of websites that you can use for this purpose, so check them out and get started!

Have you got the **millionaire mindset?**

If you think this article might include the phrase "sipping champagne on a yacht", you really should read on!

When we think about 'millionaires', most of us imagine they became rich by (a) making a killing in property, (b) inheriting a truckload of cash, (c) earning huge salaries or (d) being famous for something. The reality is much less sexy: most well-off people became that way by acting not so much like Kanye West as Kanye's accountant.

The good news is that joining the seven-figure net worth club is within the reach of most of us if we are prepared to *delay gratification and invest wisely.* Yes, this is a point worth getting worked up about.

Australia had more than 226,000 millionaires in 2014, according to the *World Wealth Report* by Capgemini. And they aren't all rich just because they bought inner-city property ten years ago: only 35% of their wealth is in property. The strength of equities markets has underpinned 22% of this wealth, a similar proportion is in cash and deposits and fixed income generates 11%.

So, how did these people get rich? Well, time and time again, research into the behaviour of the well to-do* comes up with the same key finding: the wealthy are financially conservative: they don't blow everything they earn. Basically, they drive older model cars, live in modest houses and don't splash the cash (except on education for their kids). Yep, it turns out the rich really *are* tight!

Mercer Financial Adviser, Stephen Bury, says that his experience is in line with the research. "I often encounter clients who don't earn much more than average but who have built large asset holdings and set themselves up for a really comfortable retirement."

So, what are Stephen's top tips for putting yourself in this position? "Basically," he remarks, "it's all the stuff your parents told you to do. There's no magic bullet, it's just a case of being really sensible with your money. Obviously working to a well thought-out financial plan helps."

For people in their twenties or early thirties, Stephen has the following general tips to getting started:

- Don't spend a high proportion of your income on assets like cars that lose value over time (and quickly).
- Get into the habit of saving. It's really easy to spend more and more as your salary increases, but if you do this you're not getting ahead. Instead, you might find yourself in debt, which can escalate.
- Invest for the long term and start early to use the power of compounding interest – earning interest on your interest. Super's favourable tax treatment and long term nature makes it an investment no-brainer for most people.
- Spend time on your finances: set goals, make a budget and consider paying for financial advice from the experts to set up your financial plan so you know where you want to end up and how you can get there.

If you're thinking all this sounds like one big yawn, think again. Even winning lotto isn't a sure fire ride to certain wealth. Try googling "lottery horror stories" and you'll get story after story about people who hit the jackpot winning millions of dollars but have ended up broke. The most important thing to realise is it's not how much money you have but what you do with it that makes the difference between being rich or up to your eyeballs in debt.

Frugality is back in fashion, thanks to the Global Financial Crisis, and people of all walks of life are starting to realise that not spending can be more rewarding than spending. Stephen points to Australia's current high savings rate and retail woes as evidence of this trend. "People are starting to realise that buying stuff and having all the gadgets doesn't make you happier – just poorer!"

* *The Millionaire Next Door: The Surprising Secrets of America's Wealthy (1996) by Thomas J. Stanley and William D. Danko.*

Multi-billionaire Warren Buffet (a world renowned investment guru) pays himself a base salary of $100,000 a year and lives in a modest house he bought in 1958.

'Budget' is not a dirty word

If your eyes glaze over at the mention of the 'b-word', you're not alone. "Most people will do pretty much anything to avoid preparing a budget," says Stephen, "but you can't manage your money until you know where it's actually going. It's a necessary – if sobering – part of the journey towards millionaire status."

The Scheme's website includes a Budget planner that can help you to work out what you actually spend and how much you could save or invest each month. Once you've gathered a bit of background information, you can use the tool to generate a budget in a matter of minutes. By tracking your incomings and outgoings, you may find room for some extra contributions to your super.

Contributing extra as early as possible means you can turbo charge your super because you get the benefit of a long investment timeframe and compounding interest – a powerful combination indeed!

Go to **www.samfs.superfacts.com>Planning tools >Budget planner**.

Important check list reminders

1. **Change of address**
   Have you advised the Scheme of your change of address?

2. **Nomination of Beneficiary form**
   Is your nomination of Beneficiary form up to date?

3. **Leave without pay**
   Are you going on Leave without pay?
   If so, all your insurance cover may cease.

4. **Long term sick leave**
   Members under age 60, is your sick leave due to run out?

5. **Maternity leave**
   Are you going on maternity leave and when will wages cease – as your insurances will be affected.

6. **Working less than 15 hours per week**
   For Defined Benefit Members working less than 15 hours per week, your insurance cover will be reduced to Death insurance only.

   Death insurance will cease if you are working less than 10 hours per week.

   *Please advise the Scheme on any of the above and contact the Manager, Mr Alan Kent on **8204 3826** for any clarification you may require. Information is also available in the Member Benefit Guide on the website **www.samfs.superfacts.com**

   Note: If you are on extended leave at any time, you can always access the Super Info on the website **www.samfs.superfacts.com**

7. **Salary sacrifice forms**
   Please ensure you send in **original** signed Salary Sacrifice forms to this office. We cannot process faxed or scanned copies. We need the originals to be signed off by the employer before forwarding to Shared Services.

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