a Morningstar company

Edition 383, 13 November 2020

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Editorial

One of the downsides of **Donald Trump** commanding the headlines is that we overlook more significant issues. Many Australians now know more about how the US Electoral College system works and its magic 270 threshold than they do about our own Preferential Voting system. But more important, few people have read the coverage of the **China Daily News** this week where statements are terrifying Australian producers. It says:

*"It is Canberra that has undermined what were previously sound and mutually beneficial ties by prejudicially fueling anti-China sentiment at home, baselessly sanctioning Chinese companies and aggressively sending warships to China's doorsteps ... Canberra should realize it will get nothing from Washington in return for its collusion in its schemes, while **Australia will pay tremendously for its misjudgment."** (my bold emphasis).*

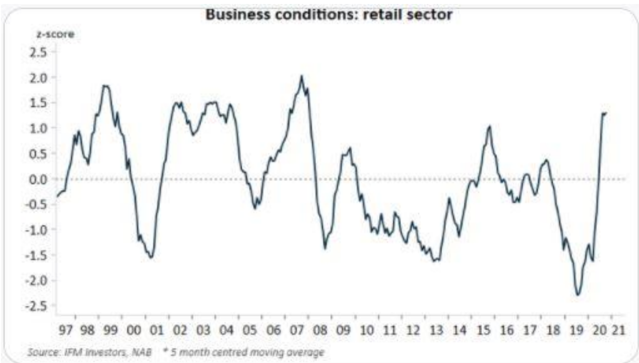
That's a bigger story for Australia than Trump, highlighted in our election update on the weekend. The article goes on to quote **Wang Wenbin**, a spokesman for the Foreign Ministry, showing it is an official Chinese view. The article continues:

"With Australia mired in its worst recession in decades, it should steer clear of Washington's brinkmanship with China before it is too late.

*To put it simply, if Canberra continues to go out of its way to be inimical to China, its choosing sides will be **a decision Australia will come to regret** as its economy will only **suffer further pain** as China will have no choice but to look elsewhere if the respect necessary for cooperation is not forthcoming."*

Dennis Richardson, former **ASIO** Director-General, speaking at an event for the **Minerals Council of Australia** this week, warned:

"I think at the moment the Australia-China relationship has got caught up with domestic politics in Australia ... we are going to be in the dog house I think for a good two to three years."



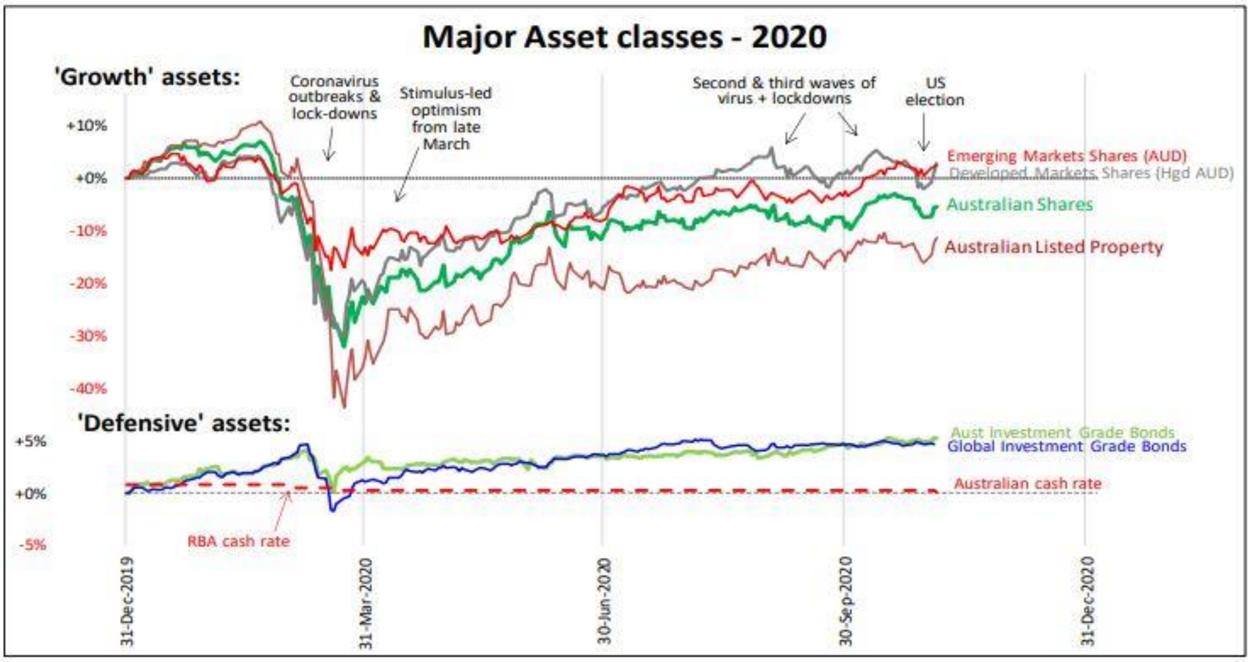
The other side of the brinkmanship is that China needs Australian products, and its much easier to ban lobsters, wine and barley than it is iron ore. How the new US administration deals with China carries implications for Australian trade.

On a more optimistic note, amid a pandemic, high unemployment and lockdowns, Australia's recovery in retail business conditions is a welcome surprise. It is supported by massive government spending, but nonetheless, few expected the best retail conditions in over a decade any time soon.

CBA Economics reports an equally optimistic measure:

"Consumer sentiment: The Westpac/MI measure of consumer sentiment showed another solid rise of 2.6% in November after a very strong lift in October. The consumer sentiment index now sits at 107.7 and well above the 100 level that separates optimists from pessimists. A reading of 107.7 is also comfortably above the long run average of 99.2. Confidence around current conditions and expected conditions continued to lift in November."

Drawing on a chart from the CIO of **Stanford Brown, Ashley Owen**, shows the stock market recovery, although Australian shares and listed property remain well below their levels at the start of 2020.



In this week's articles ...

We dive into the success of Exchange Traded Funds (ETFs) with **Alex Vynokur of BetaShares**, and explore how they performed during the pandemic and what the future brings.

Then two articles on retirement spending. First is an interview by **Michael Kitces** with the originator of the '4% withdrawal rule', **Bill Bengen**. It has become a retirement planning standard but does it still work?

Josh Funder checks the three pillars of our retirement planning system with an emphasis of the role the family home can play in meeting spending needs. He suggests a '3%+1%' as a variation on Bengen.

And while on latter-life planning, **Christine Benz** provides an intriguing list of seven estate planning items you may have missed which can make life easier for the people left behind.

Investors continue to seek alternatives to the miserable rates on cash and term deposits, which is giving bonds and hybrids a boost. **Jon Lechte** from a new sponsor of Firstlinks, **Bond income**, gives examples of new bonds available to people who qualify as 'wholesale', plus a summary of three recent hybrid opportunities. See also the announcement of the first fund in a sister business, **Fund income**.

Gold has found a place in more portfolios than ever in 2020, and **Jordan Eliseo** describes the political impact of Democrat or Republican administrations, and why gold rose then fell during the election process.

The announcement by **Pfizer** of successful vaccine trial results gave the market a kick up, but regardless of its success, in a highly competitive field, **Robert M. Almeida** finds another way to make money from the pandemic theme.

This week's White Paper from **Franklin Templeton** studies our most precious resource, water, and how it affects economic policy, population growth, climate change and the day-to-day operation of companies.

Alex Vynokur: ETFs deliver what's written on the can

Graham Hand

Alex Vynokur is Founder and Chief Executive of BetaShares, an Australian provider of Exchange Traded Funds (ETFs) with $14 billion under management.

GH: The ETF industry in Australia has not missed a beat during the pandemic, reaching all-time highs on monthly flows with balances topping $73 billion and heading for $100 billion in 2021.

AV: Yes, it's been a good year for ETFs and our business. When we were in the middle of the March volatility with COVID, it was hard to know how investors would react. But the industry overall has been really solid, and a lot of the naysayers who were casting doubt on the robustness of the ETF vehicle have been proven wrong. They were saying all is good in a bull market but just wait until volatility and market falls kick in and then we will really see what ETFs are all about. So it was great for the industry overall and BetaShares to go through such a strong experience, always trading and completely in line with our expectations. The products have delivered what they say on the can.

GH: When you started BetaShares 10 years ago, did you expect to be at $14 billion by now?

AV: We didn't have a specific funds metric in the initial business plan, rather we focused on building a business with a sustainable competitive advantage. One good thing about COVID was the chance to reflect on the overall business and ask where we will be in another 10 years, in 2030. When I think about the industry in the next decade, it will be operating at a completely different scale. It will become more 'core' in portfolios, and increasingly ETFs are the first investment many people make.

GH: In the strong growth in the last few years, has there been a particular type of ETF which has surprised you, where four or five years ago you weren't seeing the growth.

AV: Ethical investing must be called out as the x-factor for the industry and that wasn't previously on the radar. In fact, when we started the business, I didn't even know what ethical investing was, let alone that it would represent such an important part of our growth. It's only been in the last three years that the myths about ethical investing have been dispelled. The conventional wisdom was that few people would be willing to sacrifice performance for the pleasure of investing ethically. But now the track record speaks for itself in delivering performance and it's been an eye opener.

GH: How much do you have in ethical funds?

AV: Closing in on $2 billion, and just over three years ago it was zero. We have developed true-to-label investments and BetaShares accounts for the majority of ethical investment assets in the ETF industry in Australia. Increasingly, ETFs are capturing the ethical flows, which is unique, because in all other categories, ETFs have been playing catch up with active management and unlisted index funds.

GH: And the growth in fixed interest and global ETFs has also kicked in.

AV: It has as well. Fixed interest and international are great examples of the democratisation and access that ETFs deliver. Traditionally, diversification into fixed interest was the purview of large institutions, with high denominations, opaque pricing and 'over-the-counter' trading. ETFs have taken the bond game to another level, enabling all investors to connect better with the building blocks of fixed income. In the past, bond components such as governments, supranationals, credit, corporate bonds, asset backed were, for the average investor, always a mystery. ETFs have helped to demystify fixed interest, lower the cost and improve access.

GH: I remember a Chris Joye webinar around April, talking about hybrids in the fund he managers, HBRD, with spreads at historically high levels. That's turned out to be a great investment in the last six months.

AV: There's still work to do educating on fixed interest, but if you look at COVID, investors benefited from the lower volatility of bonds in their portfolios, and ETFs have delivered the outcomes they sought.

GH: Retail investors have the same access to shares in BHP or Woolworths as professional investors, but not to the wholesale bond market where most bonds are traded.

AV: Yes, and I think international shares are in the same category. Some brokerage businesses offer access to overseas shares, but global ETFs trading on the ASX give institutional pricing in this time zone without FX fees or wide spreads. So on the ASX we have a Vanguard S&P500 or a portfolio of global cybersecurity companies through HACK or NASDAQ100 through NDQ. Full transparency and costs. All investment vehicles need to deliver value and ETFs have proved themselves.

GH: On ETF product proliferation, we now have more ETFs in the US than listed companies, giving the ability to back almost any idea. Australia now has, what, 215 and a quarter of them are yours. Is this a healthy development?

AV: Well, first of all, that’s similar to saying that there are more words in the English language than letters. You can have a lot more words than letters, and you have more ETFs than individual securities. If we focus on Australia, it is a market that is far from homogenous in its participants. We have people investing for the first time, especially with the property market out of reach of the majority of young Australians today. Then at the other end of the spectrum, we have investors with significant balances, maybe in retirement, and they don't need as much growth and want strategies focused on preservation of capital. And then, the world of asset allocators who are looking for indexed building blocks for a diversified portfolio.

GH: And their needs change over time.

AV: Yes. If you’d asked me 10 years ago whether robotics and artificial intelligence would present an investment opportunity as a long-term secular trend supported by great fundamentals, I would probably not have even understood the question. The leaps that industry has made have created drivers of innovation and value creation. These are the reasons we see innovation on the product side. It will only stop if our needs as investors remain constant, and that never happens. Consider the interest rate environment that we live in today. It creates unique challenges and problems that need to be solved.

GH: I agree that the range of investment opportunities is a worthwhile development but it also means some funds will be left behind and be forced to close.

AV: Yes, but that’s absolutely fair. With an industry that's maturing, we learn from hindsight, and closing products shows an ability to make a mature assessment of what has been done well and not so well.

GH: Can you identify characteristics of ETFs which have worked particularly well, and others that have not done as well as you hoped?

AV: The most important feature is the true-to-label nature of the product that delivers an investment outcome aligned with expectations. We are experiencing a significant secular trend towards lower cost, more transparency, more liquid investments, which favours index strategies, whether those indexes are market capitalisation, thematic, smart beta or strategic beta. These deliver value to investors, whether it's the core of the portfolio, an allocation to a thematic as a satellite or tilt, whether it's a country-specific or factor based. ETFs challenge the conventional wisdom of what an index really means.

GH: And active ETFs.

AV: There is plenty of scope for both index and active to coexist, and ETFs showed the benefits of intra day liquidity in active ETFs during the extremes of COVID. The Australia market would open, say, 6% down and close 3% up. A range of 9% or 10% in one day at its extremes. Investors in an active unlisted fund had no ability to time their entry when the market was down. An order through an application form or website for the unlisted fund would be filled at the end of day price regardless of when the investment was initiated.

GH: And worth noting that the ASX’s solution to access managed funds via their platform, mFunds, is an execution service not a trading service. Investors put in an order that is filled after the close of the market, although the trade is done on the ASX.

AV: Yes, while on-market, investors could be filled immediately at a price that’s aligned with the investors' expectations. It gives more certainty on the price, whether for a buyer or seller. It's a more-evolved investment structure whether you believe in passive or active investing.

GH: BetaShares has had a lot of success with the cash product, AAA, but what’s the outlook now the cash rate has been reduced to 0.1%?

AV: AAA has grown significantly as rates have come down, and one reason is that most investment platforms now pay zero on cash deposits. People always need to have some of their balances in cash, and the relative return of AAA is probably more relevant than ever. Rates go up and down but the fund has been able to deliver rates that are more favorable than available through most cash alternatives.

GH: As recently as a couple of years ago, Listed Investment Companies and ETFs were both doing well at about $40 billion on issue. ETFs have doubled in three years and now hold $73 billion, and you are predicting $100 billion next year. What are the key differences where one has surged and the other has stagnated?

AV: The engines that power the growth of ETFs have been consistent since the beginning but the ETF industry never benefited from paying a remuneration or distribution incentive. So in the early days, ETFs were poorly adopted. Before FOFA, it was not a level playing field. The enforcement of FOFA rules through the Royal Commission has affected those structures like LICs which relied on paying for distribution. With a level playing field, ETFs prosper.

GH: If you were talking to an investor who already has the core of a portfolio covered with broad-based Australian equities, global equities, property and fixed interest, but wants to put 5 to 10% of their portfolio into something that's a little bit sexier and maybe a little bit riskier ... If you had to choose a couple of funds that you feel best about, what would they be?

AV: Two good candidates. One is Asia tech, ASIA. It's a great portfolio of high-growth companies with true bottom-up growth and innovation, such as Tencent, Alibaba and JD.com. It holds the 50 largest stocks in technology in Asia. The other one is cyber security, HACK. I think as we go cashless globally, the focus on digital wallets will demand protection of personal data, corporate data and government information. It's only just beginning and is the most exciting thematic in my view.

GH: Last question. The business has done well but what worries you the most? As Bill Gates once said, two smart guys in a garage can kill Microsoft.

AV: Yes, that's right, exactly. I ask myself what could derail the growth of ETFs, especially since at the moment, we are the disruptors of the asset management industry. ETFs make the lives of mediocre active managers miserable, but what can disrupt us? It would be a mistake to believe for a second that the ETF industry itself is immune from disruption and challenge.

That's the one thing that I am paranoid about. Not because there's anything on the horizon today but success can breed complacency. We've been blessed by our timing but we must retain the hunger, the innovative edge. A dose of paranoia about the needs of our clients and evolving with the times will prevent us becoming a dinosaur.

Graham Hand is Managing Editor of Firstlinks. Alex Vynokur is Chief Executive Officer of BetaShares Capital, a sponsor of Firstlinks. This material has been prepared as general information only, without reference to your objectives, financial situation or needs.

For more articles and papers from BetaShares, please click here.

The creator of the 4% rule and his own retirement

Michael Kitces

(This is an edited version of an interview by Michael Kitces, who is widely recognised as the publisher of the #1 financial planning blog in the United States. His website, kitces.com, is also home to the popular 'Nerd's Eye View'. See end credits for more details).

Bill Bengen is the former owner of Bengen Financial Services, an independent advice firm based in Southern California. He's known as the father of the 4% 'safe withdrawal rate' that he put into practice.

Bill discusses how he first developed the safe withdrawal rate research, the retirement problem in the early 1990s that he was trying to solve, how Bill integrated his 4% rule into his financial planning business, and why he didn't actually use the 4% safe withdrawal rate with his clients.

Michael: The research that you did around retirement withdrawals – what I think now we collectively call the 4% rule – has been around for more than 25 years since you originally published the article on it.

So talk to us now about the evolution of the 4% rule research that you did. What was going on at the time that made you say, “Okay. I want to do some research and write a paper about this and take a swing at what I think is going on with this retirement thing?”

Bill: Yes, I can tell you, the last thing I wanted to do with a fast-growing practice was to get involved in a research project that would take several thousand hours of my time, evenings, and weekends. But clients were coming to me and they were asking, “I want to save for retirement. How should I save? How much should I save? And then, when I go into retirement, how am I going to spend this money? How do I set my investments up?”

I just completed a CFP course within the last year, 18 months. That’s about 1993. And I couldn’t recall anything in any of those textbooks that addressed these issues. I spoke to people and I got a lot of different answers. There seemed to be rules of thumb based on vague experience. No one had any definitive analysis that I could find. So I said, “I guess I’m going to have to do it.” So I just got out my computer and my spreadsheet, got a copy of the Ibbotson data and started cranking numbers. That’s what it came down to.

Michael: And so, can you set the context for us at that time? What were the rules of thumb and things going around at the time that you were looking and saying, “Yeah, this isn’t cutting it, we got to go a little deeper on this?”

Bill: Well, some people said the average portfolio return is what, 7.5%? A 60/40 over time, so you should be able to take out 6%, 7%, no problem. A lot of people said, “Oh, my goodness, you’re in retirement now. You have to be in bonds, 100%. You can’t afford the risk of the stock market. What are you thinking?”

And of course, when I get into the data, neither one of those positions turned out to be viable. They were both wrong.

Michael: How did you ultimately come to this number of 4%? What made 4% the magic number that says this is the one that Bill has dubbed safe for all of us?

Bill: Well, I experimented with portfolios of different allocations and took the withdrawal rate down until I got a portfolio that lasted 30 years. And at that time, I was only working with two asset classes, basically, large company stocks and treasury notes. And I got a number of 4.15%. I created this chart and I looked at it and I said this is amazing because the withdrawal rate is the same over a very wide range of stock allocations, I think between 45% and 75%, it was about the same.

So at that point, it didn’t appear to make too much difference what you choose. But I knew that a very heavy stock allocation was bad and a very low stock allocation was bad. So I came out with a number and, of course, that number has haunted me for years since then because you know that one number cannot represent the experience of so many different retirees. There’s just too many dimensions to the problem to have a one-number solution.

Michael: And to think you went out with the thing that became so popular, people started calling it a rule of thumb and saying that’s ridiculous because it’s too generalised.

Bill: Yes, I don’t think I ever used the term '4% rule'. That was kind of a creation of the media. When I got introduced to the media, they wanted something simple to present to their readers. And they focused on that and said, “This is the answer,” like a tic-tac-toe game, put the X here.

Michael: A lot of people will point out like, “But Bill, we only get half a percent on some of our bond returns right now. When you were doing that research, you could get 6%, 7% to 8%.” It’s like, “Yes, but when you were doing the research, we were coming off double-digit inflation environments not that many years before.

So when you start looking at things like real rates of return after inflation, we may be in a somewhat lower return environment, but they’re not nearly as low a return as sometimes we make it out to be because we look at the nominal and forget the real.

Bill: Yes, I absolutely agree with that. I think it’s an overreaction. I haven’t been able to develop scenarios myself in our low inflation environment where it goes below 4.5%. So I’m not sure where those concerns are coming from. I haven’t seen the background work behind those claims, those concerns.

Michael: So I guess the big asterisk to the whole thing about 4% rule and that original research is just, today, we do have more investment opportunities. We own more than it – lower than two-asset class portfolio, large cap U.S. stocks, intermediate U.S. government bonds, and nothing else. And I guess it’s no great surprise, or as we know from modern portfolio theory, in theory, if we have more diversified portfolios, we can get better risk-adjusted returns. And I guess, when you put the safe withdrawal rate lens on it, you get a similar effect, more diversification and less volatility for a unit of risk. And then, you end up with more retirement income sustainability, and your 4% rule becomes a 4.5% rule.

Bill: One thing I noticed when I introduced the small cap stocks, because they're much more volatile asset class than large caps, where before I had a very wide plateau between 45% and 75% stocks. It narrowed it down to 50 or 60 as being the optimum equity allocation.

Michael: Interesting. So as you got more diversification in there, it kind of narrowed in like here's really the optimal balancing point of enough but not too much on the risk spectrum.

Bill: Exactly.

Michael: So I am curious then, what did this look like in practice with clients? Was this something you used in practice with clients? Was this like cool research but we still have to do it other ways when you get down to individual client's circumstances? What did the 4% rule or 4.5% rule look like for you as a practitioner with clients?

Bill: Well, when I started my practice, I didn't actually have too many clients in retirement, okay, they tended to be closer to my age and only in the later years of my practice. But clients liked the idea. They understood the basis. They read the material. They thought it was sound.

You have to be very upfront with clients and explain to them that this is not a science we're doing. Okay? It's not like Isaac Newton sitting down and developing his three laws of motion in physics, which will probably stand for billions of years into the future. What we're doing is almost a social science. We're examining the past and we have data, but we don't have an underlying theory that relates data and facts. So we can't use it to predict anything. We can only use it as a guide.

Michael: So as you went through this with clients, was the 4% rule largely your number, or did you start using 4.5% after you did your book and kind of found, "Hey, once we get more diversification here, this number goes up."? Did you have a different number you used for some clients?

Bill: I used about a 4.2% number to start. But you know every client's situation is different. I had clients that were 5.5% because they are expecting a large inheritance, let's say five years down the road, that they're fairly certain of. And I have clients who were down at 3% because they had a pension plan that had no inflation adjustment. So over time, they were going to have appreciating demands put on their portfolio to support their income stream. So, yeah, we start with four, but there's a wide spectrum around it.

Michael: As you built your business, how many clients did you find was your comfort point? When was it no more for you?

Bill: I got up to about 80 clients. I found that was about all I could handle, the real books that I had. That was a comfortable number, so I tried to keep it right around there.

Michael: Okay. So you got up to about 80 clients and kept it there. My guess is that if you leave or move or, unfortunately, pass on, you free up a few spaces. You add a few clients back in and just for you and your wife helping you in the practice that was the comfortable level of, "I can serve these clients, the income is good. We're going to hang out here."

Bill: That's right. No, even with that limited number of clients, I spent a lot of hours working nights, weekends, and I'm sure a lot of solo practitioners do that. I was younger; I've always enjoyed working hard. But if I had to do it over again, maybe I'd hold up to 60 clients.

Michael: It's the amazing thing about the advisory business, though, is just clients tend to stick around as long as we're servicing them well. They pay a pretty good dollar amount per client at the end of the day. You don't need an immense number of client relationships to have the math add up pretty well.

Bill: No, it's really, to me, it's beautiful profession. At least, it was back when I was in it. You have a very close … you feel like you're really making a difference in people's lives on a day-to-day basis, you have a direct personal contact with them, they can get you anytime they want to. And you know you have the technical skills and the support systems to do whatever they need to get done. So it's very, very, very satisfying.

Michael: And so, how long did you continue to run the practice? When did you ultimately decide you were ready to be done done?

Bill: Twenty-five years, just about, and that was 2013 when I retired. Quite frankly, I had concerns about the market, investing. I always told my clients that I would invest my money exactly as I invested theirs. As we moved into the middle of the 20 teens, I didn't think that was possible anymore. I felt I needed to get much more conservative, but I didn't want to impose that on them. Because the market could continue to go up. And so it did. So I figured I had a good run, time to cash in, go on to something else.

I did a great job when I got my clients completely out of the market in late 2008. So they never suffered the losses that other folks did. On the other side, I did a lousy job getting them back into the market after the crisis ended. If I knew then what I know now, it would have been a completely different process. But the whole financial planning profession is built around buy-and-hold philosophy, I understand that.

I think that's a mistake. I think our profession needs to be open-minded and look at alternative means of managing money and not just assume that buy and hold is the correct way to do it. Buy and hold is what I used in my analysis, my 4% rule. One thing is because it's a lot easier to analyze things than multiplicity ways you can manage money by other means. But just because I did that analysis, I told people, it doesn't mean you have to manage your money that way.

And I remember going to an FPA meeting late in November of 2008. And advisors, you know, they look like they've just been beaten to death. They didn't know what to tell their clients. They lost so much money for them. They were literally in tears. And I wasn't in that situation, which I thought was cool.

Eventually, of course, the money came back, or a lot of it. Thanks to QE. But I didn't have the process in place at that time to get back into the market. There were clear indications now, if you look at that March and April we should be heading back in there heavily.

Michael: And so, as you look at it today, you've now done literally decades of this research, you've lived it, you've lived with multiple market cycles, so I guess I'm wondering two things. One, how do you look at the 4% rule today? Is that still the number, or is it 4.5% or is it 5% or is it something else?

Bill: I think somewhere in 4.75%, 5% is probably going to be okay. We won't know for 30 years, so I can safely say that in an interview.

Michael: And you think of that paired with, it sounds like, with a more conservative allocation, at least for the time being given where valuation is?

Bill: Yeah, I think in the course of my career, to avoid large losses, yes, with the thought that if the market were to return to historically reasonable valuations, let's say, high-teens, mid-teens in the Shiller CAPE. Then I would look in to get very, very aggressive in stocks. Maybe higher than 50% to 60% I would recommend because there are very few sources of reliable income. And fixed-income investments are giving me nothing. So, I thought I'd go to 80%, 70%, 80%, 90% dividend-paying stocks if I could get them at cheap enough prices. I'm not concerned about safety. Because if you buy something at the right price, you're good for many years. So that's kind of a radical change in my view, but I think that is necessitated by the times.

Michael: And all driven by this combination of low yields, which will drive you towards more stocks but low inflation, which actually gives you comfort that we don't need to be hanging out down like 2% or 3% withdrawal rates, high 4% is enough, 5% is still reasonable because at the end of the day, when inflation is this low and you're only spending a few percent, you actually don't need a huge amount of growth in your portfolio.

Bill: No, but once you get into preserving the capital, when you retire, you've got that chunk of money, you want to preserve it; you don't want it to get diminished by any substantial amount because it may not come back. It may not.

Michael: So out of curiosity, anything you've learned as a retiree, compared to what you advised retirees – does the view look different from the other side of the retirement transition as you think about the advice you gave and now the advice you'd want to receive as a retiree?

Bill: I always told my clients, they should be thinking of retirement as moving towards something, not away from something. You're not moving away from your work life. You're working to a whole new scheme of life. And that therefore you should have things, whether it be hobbies, activities that you want to be actively involved in and know what they are. And perhaps setting the groundwork for that before you retire. I've got my writing, my research, which is part of the reason I retired. I want to have more time to do all that.

And that's worked out very well. So I feel pretty comfortable how retirement … I can't even call it retirement. I'm putting in five days a week of writing. Weekends are still meaningful to me, believe it or not. It's not all one anomalous, amorphous time span. There are weekends that are workdays. And I expect that gives meaning and structure to my life.

Michael Kitces is Head of Planning Strategy at [Buckingham Wealth Partners](), a wealth management services provider supporting thousands of independent financial advisors.

In addition, he is a co-founder of the XY Planning Network, AdvicePay, fpPathfinder, and New Planner Recruiting, the former Practitioner Editor of the Journal of Financial Planning, the host of the Financial Advisor Success podcast, and the publisher of Nerd's Eye View through his website Kitces.com, dedicated to advancing knowledge in financial planning. In 2010, Michael was recognised with one of the FPA's "Heart of Financial Planning" awards for his dedication and work in advancing the profession. This extract is reproduced with permission.

Flurry of activity in primary bond markets

Jon Lechte

Retail investors have ready access to the shares of over 2,000 companies listed on Australian securities exchanges (ASX and Chi-X) and can easily trade equities in small amounts through stockbrokers, including online execution. In contrast, most fixed interest securities are classified as 'wholesale' and are traded in the 'over the counter' (OTC) market through brokers, fixed interest dealers and institutions rather than on a listed exchange.

However, it is possible for some retail or non-professional investors to access OTC wholesale securities, which offer a wide range of credit qualities, structures, and maturities. In an era of low interest rates and uncertainty over COVID, more investors are seeking investments with a higher return. They are checking whether they are eligible to become certified as wholesale investors, as well as learning how bonds work. As investors look for greater portfolio diversity and stable fixed income options, fixed income investment solutions are more on the radar.

Generally, the definition of a wholesale investor in the Australian market is a person certified by a qualified accountant to have:

- A gross income of $250,000 or more per annum in each of the previous two years, or
- Net assets of at least $2.5 million.

Unlisted (OTC) primary issuance

October 2020 was a good example of the types of securities available in a busy month for primary markets. As well as secondary market trading in existing securities, the Bond income team was active in many initial bond offerings across a wide spectrum of fixed income, including ESG compliant/Green bonds, high-yield bonds and AAA-rated supranational and semi-government issuers. Issuers took advantage of favourable market conditions, whilst at the same time bringing forward transactions to avoid any complications around the U.S. election and typical late-November competition for capital before the holiday season lull.

Amongst the most popular for investors was the Lend Lease-certified Green Bond. The 7-year note (October 2027 maturity) priced with coupon of 3.40% was investment grade rated by both Moody's and Fitch. The primary order book was greater $1 billion versus the total issue size of $500 million. As a result, the bonds have already appreciated in price to approximately $101.50, thus providing early capital gain performance for investors. Moreover, the large order book highlights the significant demand for ESG-compliant assets amongst a rapidly increasing pool of capital active in the ethical investment sector.

High-yield investors also took up the Bennelong Funds Management senior secured bonds with enthusiasm. The $25 million unrated deal sold quickly with investors attracted to the deal by the high 10% coupon and short term to maturity of three years. There was good brand recognition with Bennelong a highly-regarded fund manager in Australia. The high return offered to investors was a reflection of the two main risks – asset coverage and secondary market liquidity. The bonds were secured at the holding company level, not at the fund level. Thus, investors hold security over the underlying equity ownership of the funds not the assets of the fund. Moreover, given the issue size of just $25 million, liquidity before maturity will be limited.

ASX-listed diversified financial services company ClearView Wealth (ASX:CVW) issued its inaugural wholesale subordinated (Tier 2) floating rate note at 90d BBSW+6.00%. The bonds mature in November 2030 but are callable at the issuer's discretion in November 2025. Despite the security rating below investment grade, lenders appreciated the APRA-regulated nature of the company and the relatively high initial margin, with a coupon which resets every 90 days.

Active listed hybrid issuance

The ASX-listed hybrid market was also busy with Challenger, Bendigo Bank, and Bank of Queensland all seeking regulatory capital via additional tier 1 issuance. The deeply subordinated hybrid securities offered investors franked coupons paid every 90 days. All three issues were also used to refinance existing hybrid securities.

Our research partners, [BondAdviser](), provides the following commentary:

- **Bendigo and Adelaide Bank Limited** (ASX:BEN) launched an offer for Bendigo and Adelaide Bank Capital Notes (ASX:BENPH) to raise $350 million, with the ability to raise more or less. The offer is accompanied by a Reinvestment Offer for holders of Bendigo and Adelaide Bank Convertible Preference Shares 2 (ASX:BENPE). The proceeds will be used to fund the redemption of BENPE and for general corporate purposes. It may also be used to fund the redemption of Bendigo and Adelaide Bank Convertible Preference Shares 3 (ASX:BENPF), which have a first call date on 15 June 2021. These securities are structured as unsecured, subordinated, perpetual convertible notes. Distributions are discretionary, non-cumulative, floating rate, expected to be fully franked and paid on a quarterly basis in arrears until converted or redeemed. The margin is guided at 3.80% to 4.00% p.a. above 90-day BBSW.

- **Bank of Queensland Limited** (ASX:BOQ) launched an offer for Bank of Queensland Capital Notes 2 (ASX:BOQPF), to raise $200 million, with the ability to raise more or less. These securities are structured as unsecured, subordinated, perpetual convertible notes. Distributions are expected to be discretionary, non-cumulative, floating rate, fully franked, and paid on a quarterly basis in arrears until converted or redeemed. The margin is guided at 3.80% to 4.00% p.a. above 90-day BBSW.

- **Challenger Ltd** (ASX:CGF) launched an offer for Challenger Capital Notes 3 (CCN3, ASX:CGFPC), to raise $250 million, with the ability to raise more or less. The offer is accompanied by a Reinvestment Offer and Repurchase Invitation for holders of the existing Capital Notes 1 (CCN1, ASX:CGFPA). These securities are perpetual, unsecured, convertible, redeemable, subordinated notes. The purpose of the transaction is to raise regulatory capital (Additional Tier 1) for Challenger Life Company Ltd (CLC). The margin is guided at 4.60% to 4.80% p.a. above 90-day BBSW and distributions are expected to be initially partially franked, floating rate, discretionary, non-cumulative, subject to Payment Conditions and paid on a quarterly basis in arrears.

  This security has no fixed maturity date but is scheduled for mandatory conversion into CGF ordinary shares on 25 May 2028, or later when conversion conditions are satisfied. At the Issuer's discretion, and subject to approval by APRA, the Notes may be redeemed or resold for cash or converted into CGF ordinary shares on 25 May 2026. The Notes may also be redeemed if a Tax or Regulatory Event occurs. The Notes will convert into CGF ordinary shares following an Acquisition Event, subject to conversion conditions.

Despite the constant COVID-19 risks and potential market headwinds generated from the US election, credit markets have remained firm. This chart is the Australian ITRAXX, an index of credit default swaps for the most liquid investment grade Australian bond issuers. The index is a proxy for the health of domestic credit or fixed income markets. The chart highlights the huge spike in perceived risk at the height of COVID-19 market panic, followed by a sustained recovery and subsequent narrowing of the average credit margins.

Moreover, Australian base interest rates are now incredibly low on a historical basis (10-year interbank swap rates range from 0.04% for 1 year to 0.77% for 10 years). The additional return provided by the credit margin in non-government bonds or floating rate notes means fixed income markets offer alternatives for eligible investors looking to boost overall portfolio returns.

Jon Lechte is Chief Executive Officer at [Cashwerkz](). [Bond income](), a sponsor of Firstlinks, provides access to fixed interest securities for wholesale investors (certified by their accountants) and eligible Australians including financial advisers with wholesale clients. Securities offered include global fixed income, OTC and listed debt securities and new issues from a broad suite of issuers (investment grade, sub-investment grade and non-rated issues).

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Amid vaccine hope and skepticism, testing is key

Robert M. Almeida

with Nicholas A. Demko and Matthew Scholder

Editor's note: This article was written shortly before US pharmaceutical company Pfizer announced its vaccine is "more than 90% effective in preventing COVID-19 in participants". Such an excellent result means that for every 100 people who catch COVID-19, only 10 will remain ill.

Morningstar analysts, Damien Conover, wrote this on 10 November 2020:

"With the vaccine's efficacy over 90% and no major safety issues observed, we believe the regulatory agencies are likely to authorise it for emergency use in late 2020, followed by full approval in 2021 pending supportive final data. The US Food and Drug Administration has said it would need at least 50% efficacy to approve a covid-19 vaccine, and BNT162b2 clearly passes this threshold. Further, the lack of major safety issues should reassure regulators and the general public. With manufacturing ramping up, the firms expect to produce up to 1.3 billion doses in 2021."

However, Pfizer made the announcement in a media release based on a study lasting a few months and the results are not peer reviewed independently. While such progress is a great sign, the following article remains relevant.

Financial markets are betting big that one or more successful coronavirus vaccines will help society return to normal but with vaccines come multiple challenges, not least of which is people's willingness to be vaccinated.

In our view, mass testing is needed until vaccines and therapeutics are widely available and accepted. As a result, companies in the life sciences supply chain may offer sustainable investment opportunities.

Multiple entries, hopefully multiple winners

Most vaccine markets are monopolies or duopolies, but in the case of COVID-19, the World Health Organization reports that there are 42 vaccines in clinical evaluation and over 149 in preclinical development. This is a multi-horse race, hopefully with multiple winners. It goes without saying that we hope this becomes an overcrowded market with immense competition and success for all involved.

But let's look at this through an investment lens.

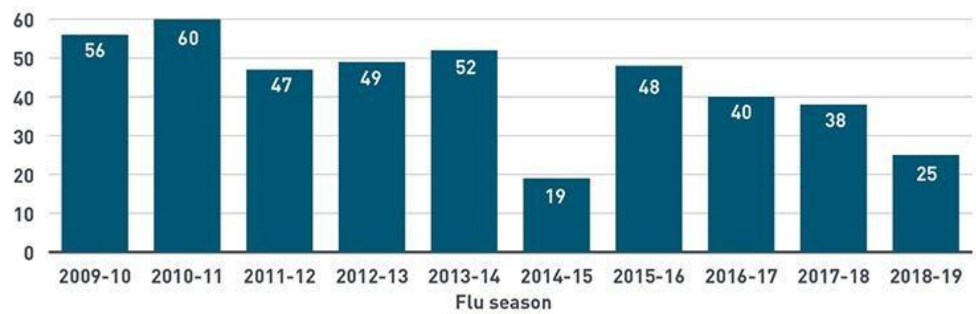
The entire global vaccine market generates approximately $30 billion annually. As optimism over the creation of successful coronavirus vaccines has grown, investors have priced a lot of it into biopharma stocks, adding nearly $100 billion to their market capitalizations. If asset prices are a reflection of future cash flow probabilities, the market has discounted optimistic outcomes such as successful drug discovery, price durability and recurring revenue.

However, following regulatory approvals, vaccine makers face mass production and distribution challenges. For example, China and India manufacture the bulk of the world's vaccines, presenting the potential for bottlenecks. As well, limitations in airfreight capacity or the need for temperature-controlled delivery may slow distribution, particularly in warm-weather regions such as Africa, Asia and Central America.

Effectiveness of vaccines

Manufacturing and distribution issues aside, there is a meaningful likelihood that efficacy rates will not bring herd immunity at any time soon. Exhibit 1 below is a 10-year look-back at the effectiveness of flu vaccines in the United States. Efficacy is low and has been falling for the past several years.

Exhibit 1: Flu shot efficacy diminishing



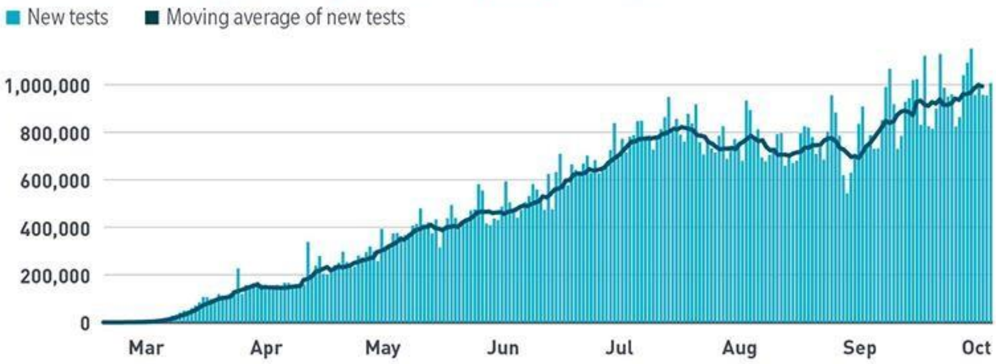
Source: As of 2019: Source: US Centers for Disease Control and Prevention.

Additionally, under normal circumstances, a portion of society is typically skeptical of new vaccines. And given the politicisation of this disease, the percent of the population unwilling to be inoculated may be larger than normal. Hypothetically, a COVID-19 vaccine with 50% efficacy (applying a simply average from the chart above) consumed by 50% of the population would immunize only 25% of the population. While this is a simple assumption, it is material, as a 25% immunization rate would be well short of the 70% to 90% minimums often cited by epidemiologists as necessary to achieving herd immunity.

This is why society needs more COVID-19 testing. While these significant challenges — from drug discovery, to manufacturing and distribution, to garnering societal trust — are addressed, identifying those infected and isolating them early can prevent or limit contagion. Although therapeutics will accelerate recovery times and reduce hospitalizations, society will still need a step-function jump in testing.

Testing capacity has grown a lot, as shown in the Exhibit 2. According to The COVID Tracking Project, the US saw exponential growth in testing during the spring and early summer. While the rate of growth has decelerated recently, the recent seven-day moving average is just under one million tests a day. That still isn't enough.

Exhibit 2: Testing growing, but not quickly enough



Source: COVID Tracking project, as of 14 October 2020.

According to a report by Duke University and The Rockefeller Foundation, asymptomatic people transmit approximately 30% to 60% of cases. The report concludes that given current infection rates, the US needs around 200 million tests a month compared with the current trend of about 25 million. Given a reasonable possibility that we will be experiencing meaningful community spread of the virus for some time to come, the best approach to resuming "normal" life would be mass testing.

With focus on vaccines, test manufacturers underappreciated

We think investors may be underappreciating the opportunity for COVID- 19 test manufacturers and services companies.

To be transparent, we have been overweight higher-quality life science instrumentation, medical device and related service companies for many years in several equity strategies. In general, we think these companies offer attractive long-term investment attributes such as:

- a 'razor/razor blade' recurring revenue model in which, following the sale of instrumentation, comes a high-margin, predictable revenue stream from consumables and reagents
- a scientific customer base that values quality, features and accuracy over cost and that encourages innovation and can command a premium price
- diverse and niche end-markets that enable only a handful of innovative companies to dominate market share in their product categories

We believe these three characteristics create sustainable, long-term economic moats that manifest themselves through a relatively strong return history and lower earnings volatility.

A handful of the largest life science companies not only develops, manufactures and distributes the global supply of COVID-19 testing supplies but also develops, manufactures and quality-checks vaccines and therapeutics. We don't think it's a coincidence that the current management of the virus through testing and the future management of the virus through vaccination are enabled by the same kinds of highly innovative companies that support modern scientific advancement.

Simply put, we believe companies in the global life sciences supply chain will create more sustainable profits than those in the highly-competitive vaccine market. While much of the current testing-related sales will be one-time in nature as society manages through the pandemic toward mass vaccination and natural immunity, the investments, innovation and future growth fueled by short-term virus-related revenues will potentially enable these companies to build on their long histories of investing in innovative, sustainable and high-returning endeavors.

Robert M. Almeida is a Portfolio Manager and Global Investment Strategist, and Nicholas A. Demko and Matthew Scholder are Equity Research Analysts at MFS Investment Management. The views expressed are those of the author(s) and are subject to change at any time. These views are for informational purposes only and should not be relied upon as a recommendation to purchase any security or as a solicitation or investment advice from the Advisor. No forecasts can be guaranteed. This article is issued in Australia by MFS International Australia Pty Ltd (ABN 68 607 579 537, AFSL 485343), a sponsor of Firstlinks.

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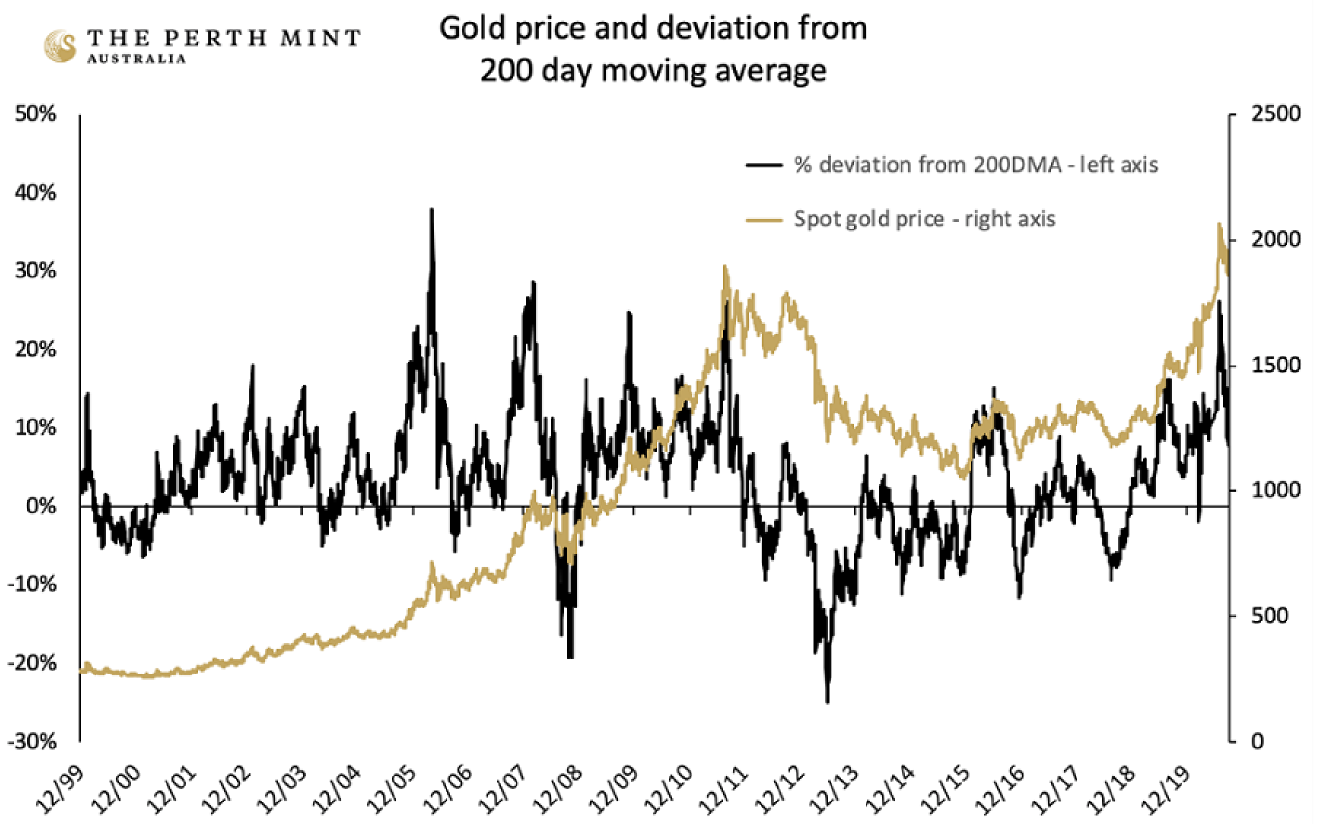
Republican or Democrat - does it matter for gold?

Jordan Eliseo

It's been just over three months since the gold price traded at all-time highs in nominal terms, hitting US$2,067 per troy ounce on 6 August 2020.

Despite the many tailwinds that drove the gold price to that level, an examination of market history suggested there was too much investor exuberance on the long side of trade at the time and that a period of consolidation was required.

This is evident in the chart below, which plots both the USD spot price of gold and how far the spot price was trading above or below its 200-day moving average (200DMA) on any given day. Data covers from the end of 1999 through to the end of September 2020.



Source: The Perth Mint, Reuters

The chart highlights that there have been several occasions in the past 20 years (in 2006, 2008, 2009 and 2011) when the gold spot price was trading at 20% or more above its 200DMA, which is where it sat in early August of this year.

On each prior occasion that the market ran this hot, it was soon followed by a period of consolidation, declining in the following three months by an average of approximately 10%.

Almost exactly the same thing has happened again this time around. In what was, in many ways, a textbook correction leading into the early November US Presidential election, gold ended October 2020 trading at USD 1,881.90 per troy ounce, 9% below the August 2020 all-time high.

Gold and US Presidential elections

The gold price rallied in the days after voting closed for the 2020 US Presidential election, trading at more than USD 1,950 per troy ounce late last week, up more than 3% from the October close. This proved short lived, with the precious metal falling close to USD 100 per troy ounce on news Pfizer may have successfully developed a COVID-19 vaccine.

As for what happens next, a review of the performance of gold in the aftermath of prior US Presidential elections is one (admittedly imperfect) way of getting a feel for how the precious metal may perform in the period ahead.

Our own analysis based on market movements in the aftermath of every US Presidential election since 1968 suggests that the gold price has on average risen by 5.58% in the year after each election.

There is however a wide disparity within the one-year figures, with a best result of +51.83% (after the 1972 election), while the worst result saw gold deliver a return of -32.67% (following the 1980 election).

The table below highlights the average, the best and the worst returns over one, three and five years for the USD gold price in the aftermath of every US Presidential election since 1968.

Gold price returns			
Timeframe	**Average return**	**Best return**	**Worst return**
1 year	5.58%	51.83%	-32.67%
3 years	42.99%	203.42%	-40.52%
5 years	81.66%	342.31%	-49.16%

Source: The Perth Mint, Reuters

State Street global advisors also analysed the performance of gold in various US political environments. Rather than look at one, three and five year returns in the aftermath of each election, they instead looked at average annual returns for gold based not only on which party occupied the White House, but who controlled the US Congress.

The results are displayed below.

	Party in control	Average annual return (%)
Presidency	Democrat	11.2
Presidency	Republican	10.2
Congress	Democrat	20.9
Congress	Republican	3.9

Source: State Street Global Advisors

The data suggests that whoever occupies the White House has little to no material impact on gold price returns. The table shows that the gold price delivered annual average gains of 11.2% under Democratic Presidents and 10.2% under Republican Presidents.

The data instead indicates that it is far more important who controls the US Congress. The gold price has historically risen by more than 20% per annum under a Democrat-controlled US Congress, in comparison to an increase of just 3.9% under a Republican-controlled US Congress.

Interestingly, the worst environment for gold has been when the US Congress isn't controlled by either party. In such environments, the gold price only saw average annual increases of 3.5%.

Ignore the election noise

While the above analysis provides some interesting insights, it is no guarantee of what will transpire in the years to come.

As such, we think investors are better served focusing on the other macroeconomic, monetary and market forces that may impact their portfolios going forward. In doing so, we believe many will conclude that irrespective of the US political environment, there are multiple factors supporting gold and the role it can play in a portfolio.

Monetary policy remains a key tailwind, with the decision last week by the Reserve Bank of Australia to cut interest rates, target lower bond yields and launch an AUD 100 billion Quantitative Easing program an illustration of how much easy money will be injected into the financial system in the years to come.

Real rates on cash and much of the fixed income universe will remain negative for years to come.

Gold should also be supported by investors looking to hedge against equity market risk, which remains high. This is driven by multiple factors, including:

- The continued threat posed by COVID-19, the spread of which has worsened in developed market economies in the Northern Hemisphere over the past month. Pfizer's news about a vaccine is a welcome development, but it's not an immediate cure to the pandemic.
- Equity market valuations, which remain stretched by historical standards.
- Potential for ongoing political gridlock in Washington.

Trade tensions are also likely to remain, even if the rhetoric is dialled down with a change in the White House. These ongoing pressures, coupled with the supply chain concerns posed by COVID-19, suggest that inflationary risks may be more apparent than the market is currently anticipating, despite the very real demand deficit that exists in the global economy today.

Jordan Eliseo is Manager of Listed Products and Investment Research at [The Perth Mint](), a sponsor of Firstlinks. The information in this article and the links provided are for general information only and should not be taken as constituting professional advice from The Perth Mint. You should consider seeking independent financial advice to check how the information in this article relates to your unique circumstances.

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Home equity access and four challenges of retirement

Joshua Funder

Australian Baby Boomers are among the world's wealthiest, yet they experience widespread retirement funding insecurity due to inadequate access to the three pillars of our retirement funding system:

- the age pension and social security system generally
- superannuation
- voluntary savings, including home ownership.

Our pension system is means tested, adjusting for variations in our non-housing wealth over time. In our superannuation savings system, however, Baby Boomers only began contributing 3% to their super half-way through their working lives.

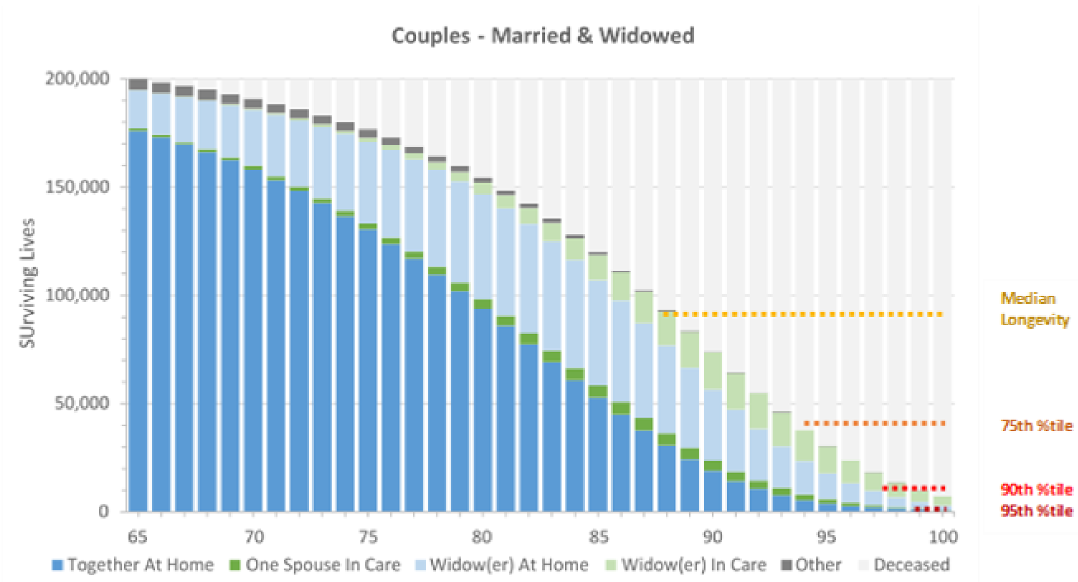
For most, the bulk of wealth is stored in the family home. Retirees need to plan for long lives at home for 25 to 30 years in retirement. Few want to downsize or prematurely enter aged care. For many Australians, the question is how to fund their long lives at home with confidence.

New opportunities to fund retirement

So, the challenge is to support retirees by providing funding, housing, care and community throughout retirement to ripe old age.

Here are some new rules of thumb that can draw on all three pillars of retirement funding and meet the needs of the vast majority of retired Australian homeowners.

1. The longevity challenge of retirement



Australians enjoy remarkably long and healthy lives. An average Australian couple aged 65 can expect to be alive together for some 20 years and for the surviving spouse to live into their late 90s. This extended longevity brings both opportunity and challenge for Australian retirees with the uncertainty of knowing how much money is needed to provide for a comfortable retirement.

2. The housing challenge of retirement

Most older Australians wish to remain at home throughout retirement. Recent retiree research confirms that around 75% of homeowners aged 60+ wish to remain in their own home, leaving just over a quarter intending to downsize.

The recent pandemic experience has challenged the health, finances and confidence of a generation of older Australians. The Royal Commission into Aged Care, in combination with the high incidence of COVID mortality and morbidity in aged care facilities, has reinforced the overwhelming desire to age in place.

While many government policies are aimed to support in-home ageing – and in-home ageing is both popular and more cost efficient than institutional aged care – the overall funding of aged housing and aged care by government alone is insurmountable.

Part of the answer must involve recognising the fundamental dual role of the family home in both housing and savings. Another part is to allow retirees to better access to manage their wealth to fund their own retirement.

3. The funding challenge of retirement

Traditional approach: 4% drawdown

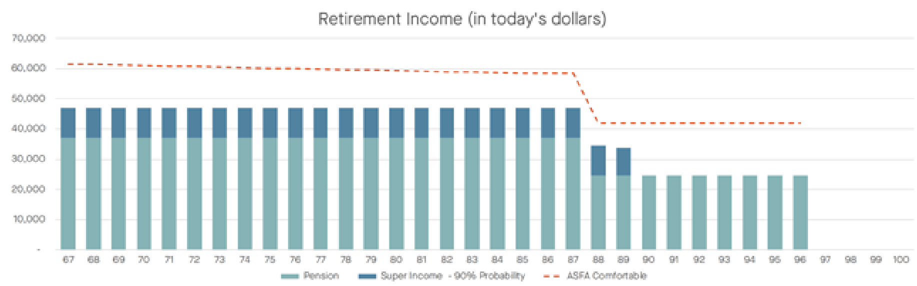
In the early 1990s, William Bengen demonstrated that an annual drawdown of 4% of savings at retirement each year would improve the chances that those savings would last 30 years. Around the world, variations of the 4% rule of thumb have often been used as the 'safe withdrawal rate' to ensure pension sustainability.

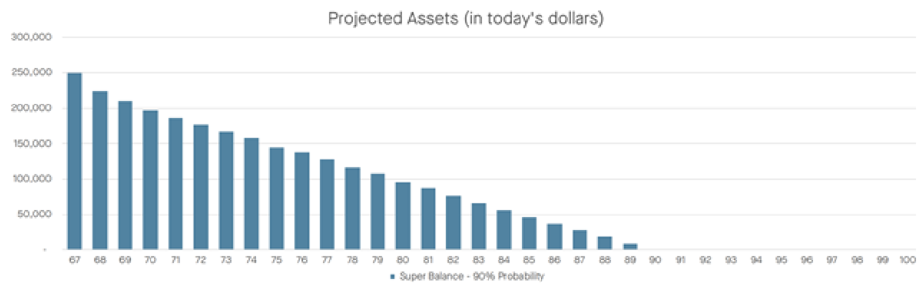
Since then two major changes have challenged the ability of the 4% rule to generate a sustainable retirement income: longevity has increased significantly over the past 30 years and we are now facing a significantly lower growth environment, with reduced interest rates, dividends and portfolio appreciation.

Let’s take the case of a retired couple, both 67 years of age with $250,000 in superannuation and owners of a $750,000 home trying to fund their retirement. The new reality of the long term, low growth outlook they face is: 5% pa returns on superannuation growth, 0.75% pa paid in fees to manage their investments and 6% pa investment volatility.

House price growth is 3% pa long term, with 3.5% estimated volatility of house prices and 5% pa home equity access cost. Long-term inflation is 3% pa. How can they navigate the next 30 years?

Scenario 1 – Drawing 4% a year of super in a low growth environment provides only 20 years of an inadequate income with the surviving partner living without any super





Clearly the 4% rule doesn't go the distance and the couple's retirement savings run out well before their expected longevity. These approaches have only been applied to the question of how to draw down a superannuation or investment portfolio balance.

In this 4% drawdown example, the couple were forced to live on a retirement income consistently well below the ASFA 'comfortable' standard and the surviving partner lived on the pension alone for the last seven years. The couple had little flexibility to maintain a quality lifestyle, manage unanticipated expenses like healthcare and in-home care, or even to fund and enjoy extended longevity.

The Australian retirement funding conundrum: drawing on all three pillars

Jane Hume, Assistant Minister for Superannuation, Financial Services and Financial Technology recently stated:

The third pillar, or voluntary savings, is incredibly important to the retirement security of Australians. For many, as we know, the family home is possibly the most significant form of voluntary savings that retirees have historically had, because retirees have historically had a very high level of home ownership compared to other countries than Australia. However, the family home is not actually considered a part of a person's retirement income.

The solution to this conundrum is arguably simple: access some of the home equity to improve retirees' lifestyles. Australians, however, have no widespread experience of responsible, long-term access to home equity as part of wealth management and retirement funding. Quite simply, our system has not provided universal access to all three pillars of the retirement funding system.

The preceding challenge notwithstanding, there is hope on the horizon in new forms of home equity access that allow borrowers to release modest amounts of home equity on an ongoing basis, as well as provide flexible access to anticipate financial contingencies throughout retirement.

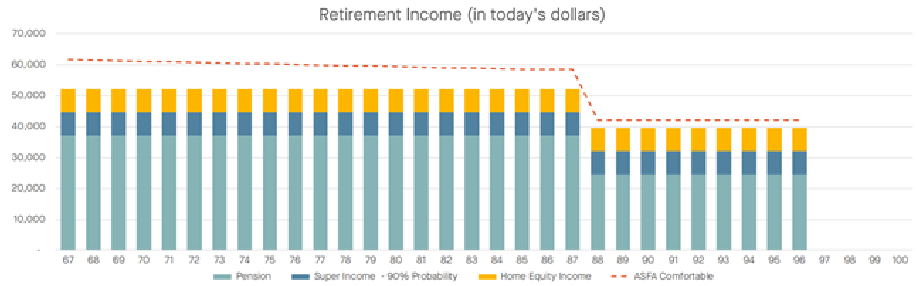
A new approach: 3+1% drawdown

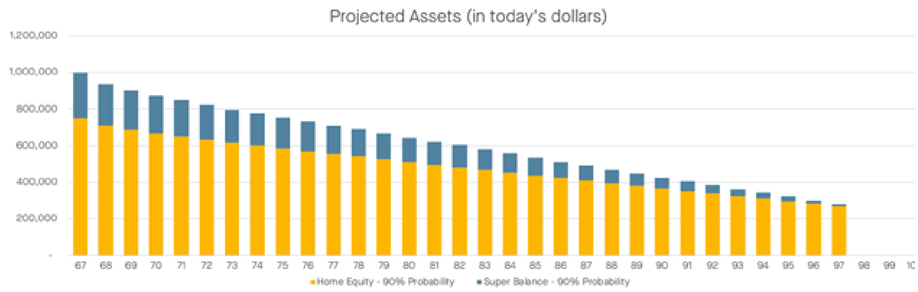
Australian retirees are among the wealthiest in the world, with average wealth per household over the age of 65 years an eye popping $1,400,000. But in most cases, around $1 million of that wealth is stored in the home where the couple want to stay throughout their retirement.

Instead of the old 4% drawdown rule of thumb, to get through retirement with confidence, Australian retirees should use a 3+1% drawdown rule: draw down 3% of the value of your investments at retirement per year plus 1% of the value of your home equity per year.

By reducing the superannuation drawdown rate and adding an additional 1% per annum draw down from home equity, our couple could begin to achieve a retirement income that is both sustainable over more than 30 years and adequate relative to comfortable lifestyle standards.

Scenario 2 – Drawing 3% a year of super and 1% of home equity in a low growth environment provides lifelong and adequate income with additional available access to capital





Using a 3+1% retirement drawdown approach also provides our couple with the flexibility to draw additional funds along the way if they need to renovate the home, meet unexpected expenses, if they live longer than anticipated or they choose to give to their children and grandchildren before they die.

4. The challenge of a sustainable retirement

In providing a path to a sustainable and adequate retirement, the 3+1% rule of thumb has major implications for Australian retirement funding:

- 3+1% provides a sustainable and adequate retirement funding plan for the majority of Australian retirees, not just those with $1 million in super
- 3+1% would improve retirement outcomes, lifestyles, and wellbeing
- 3+1% helps Australian retirees drawn on all three pillars of retirement funding flexibly throughout retirement to meet their own retirement funding needs
- 3+1% harnesses the value of the family home for both retirement housing and funding
- 3+1% diversifies retirees' sources of retirement funding and improves the probability they will successfully fund their full longevity.
- 3+1% preserves significant savings for retirees to be the bank of mum and dad and to bequeath to the next generation without unduly depleting available retirement funding
- 3+1% supports age-appropriate housing for in-home ageing at all stages of retirement for couples and surviving partners
- 3+1% maintains a significant reserve of value to fund in-home care and residential aged care
- 3+1% would boost retiree consumption and provide a long-term stimulus to the local economy
- 3+1% brings $1 trillion of retirees' savings to bear on funding their own retirement without including the home in the assets test for the pension or imposing a death tax to recoup the costs of aged care services.

Joshua Funder is Chief Executive Officer of Household Capital. This analysis and the charts were created by Household Capital Pty Ltd using data from the ABS 2016 Census combined with mortality information from the Australian Government Actuary and Household Capital internal company data. Nothing in this report provides any form of financial advice.

Seven items your estate plan may have left out

Christine Benz

If your goal is to look out for your loved ones, consider tackling these estate-planning additional jobs.

Estate planning is the easiest financial planning to-do to put off. It's certainly not fun to ponder your own mortality, and yet that's the very nature of estate planning. Lawyers are often involved, so it can be hard to get it done on the cheap. And while most financial planning jobs provide at least some payoff during your lifetime, estate planning isn't as much for you as it is for your loved ones.

It's no wonder that so many individuals put off creating or updating an estate plan. But anecdotally, at least, the pandemic seems to be lighting a fire under some people to get serious about creating or updating their estate plans once and for all.

Making sure you have the key estate planning documents in place is important; that means a will, powers of attorney for healthcare and financial matters, and guardianships for minor children, first and foremost. Trusts may also make sense in certain situations. But there are other add-ons that you can think about in the context of your estate plan, especially if your goal is to make life as easy for your loved ones as possible and to ensure that your wishes are carried out after your death. In contrast with a traditional estate plan, you can craft at least some of these documents on your own, without the aid of a solicitor.

1. A financial overview

In my parents' later years, I was intimately involved and eventually in charge of their finances, managing their investments, paying their bills from their bank account, and so on. When they eventually passed away, I didn't have to hunt around for key documents or climb a learning curve about their finances.

But many of us don't have or want that kind of backup in place, which is why I think it can be helpful to create a financial overview and master directory for your loved ones. (These documents can also come in handy if you're the main financial decision-maker in your household and your spouse doesn't pay too much attention.)

A financial overview and master directory go hand in hand.

I recently created such a financial overview for our household and included the following headings:

- Our estate plan (in very broad terms: where to find the documents and who the key agents are - POAs and executors).
- Our key financial assets (no dollar amounts or account numbers; just where we hold the accounts and who owns them).
- Our insurance coverage (property/casualty, health, life).
- Our house (property ID number, whether there's a mortgage).
- Cars (VIN numbers, whether there are car payments).
- Regular household bills that we pay.

2. A master directory

Think of a master directory as a detailed version of your financial overview. Whereas the financial overview is a Microsoft Word document, this is the Excel version. For example, your financial overview might say, "We are each members of the Jill and John Self-Managed Superannuation Fund." But the master directory would include the actual account numbers for those accounts, the URLs, and the names of any individuals you deal with at those institutions. Because the master directory includes sensitive information, it's crucial to encrypt it or, if it's a physical document, to keep it under lock and key.

3. A plan for your personal property

Most wills will state that any tangible personal property, like furniture, should be sold and the proceeds added to your estate. But if you have sentimental or valuable items that you'd like to earmark for specific individuals, such as jewellery, artwork, or special home items, you can also create a memorandum of tangible personal property that specifies who you would like to inherit those items.

For your own sanity, don't go overboard in earmarking every little thing for specific individuals; focus on those items you treasure that will also have meaning for the recipients. I found that creating such a memorandum – and matching my favourite possessions to the loved ones in my life who I thought would appreciate them the most – to be one of the most enjoyable and cathartic aspects of the whole planning process.

In addition, because the memorandum isn't technically part of your will, you can update it as you obtain or shed possessions (or loved ones!). Such a memorandum is legally binding in most states, as long as it's mentioned in your will. But even if the memorandum isn't legally binding, it's probably still worth doing and assuming that your loved ones will honour it.

4. A plan for your pets

If you're an animal lover, you know that pets aren't possessions; they're part of the family. Thus, more and more estate plans include provisions for pets. There are a few ways to incorporate pets into an estate plan, and they're a gradation.

The gold standard, albeit one that entails costs to set up, is a pet trust. Through such a trust, you detail which pets are covered, who you'd like to care for them and how, and leave an amount of money to cover the pet's ongoing care.

Alternatively, you can use a will to specify a caretaker for your pet and leave additional assets to that person to care for the pet; the downside of this arrangement is that the person who inherits those assets isn't legally bound to use the money for the pet's care. At a minimum, develop at least a verbally communicated plan for caretaking for your pet if you're unable to do so.

5. A digital estate plan

Even people who think they've ticked off all of the usual boxes on their estate-planning to-do lists may have overlooked an increasingly important component of the process: ensuring the proper management and orderly transfer of their digital assets after they die or become disabled.

Just as traditional estate planning relates to the management and transfer of financial accounts and hard assets, digital estate-planning encompasses your digital possessions, including the tangible digital devices (computers and smartphones), stored data (either on your devices or in the cloud), and online accounts such as Facebook and LinkedIn. The laws around digital assets are changing quickly, and different providers have different policies/levels of access. But a key first step is taking an inventory of all of your digital accounts and storing it in a secure but accessible location.

You can include it as a separate sheet on your master directory, discussed above. Discuss the existence of this document with your executor, and if you have valuable digital assets (cryptocurrency, for example) you'll want to be sure to discuss them with your attorney and incorporate them into your formal estate plan.

6. A plan for the end of life

If you'd like to add additional background for your spouse, children, or other loved ones who might be making healthcare decisions on your behalf, check out "The Conversation Project". It offers a starter kit to help you clarify your thinking and discuss these matters with your loved ones.

It's also worthwhile to spell out your wishes and any plans you've made for funerals, memorials, and the disposition of your body, either verbally, in writing, or both. Maybe your wishes are simply to have your loved ones say goodbye in whatever way gives them the most peace at that time; in that case, tell them that or write that down.

7. An ethical will

Consider writing or recording an ethical will that spells out your beliefs and values. In contrast with a conventional will, which lays out how you'd like your financial and physical property to be distributed, an ethical will is a way to 'hand down' your belief system to your loved ones.

The tradition of ethical wills began in the Jewish community but it has gained more interest across cultures over the past decade. This is a heavy assignment, so don't put too much pressure on yourself to be profound or to write an ethical will all at once. Instead, consider starting your ethical will by jotting down your beliefs as they occur to you. To help remove some of the pressure, balance light bits of wisdom with the deeper life lessons that you've learned.

Christine Benz is Morningstar's Director of Personal Finance and author of 30-Minute Money Solutions: A Step-by-Step Guide to Managing Your Finances and the Morningstar Guide to Mutual Funds: 5-Star Strategies for Success. This article does not consider the circumstances of any investor, and minor editing has been made to the original US version for an Australian audience.