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QUARTERLY INSIGHT

InterPrac Financial Planning Newsletter Winter 2017

Adjusting Retirement Expectations

The world is changing and retirement is changing with it.

A recent global survey conducted by HSBC (The Future of Retirement Shifting Sands 2017 by HSBC Holdings plc) has found that overall, around two-thirds of working age people are concerned about declining state pensions/ social provision and the growing number of older people requiring retirement funding/support, alsi believing that levels of national debt mean there will be less support for the elderly. Almost a quarter of working age people believe government pensions will no longer exist when they come to retire, and unsurprisingly this view is more common among Millennials than Baby Boomers.

Only 21% of working age Australians believe they will be financially comfortable in retirement. Of those surveyed:

- 58% believe they will have to work longer and continue working to some extent in retirement;
- 75% were willing to defer retirement for two years in order to have a better retirement; and
- 65% are concerned about declining state pensions, like the Australian age pension, because of mounting national debt and an ageing population.

The report goes on to set out some practical steps when planning for retirement. While these are more directed towards the Millennials, to an extent, they apply to all generations:

- Be realistic – start saving earlier, and save more;
- Consider different sources of funding – balance savings to spread risks and maximise returns;
- Plan for the unexpected – include worst case scenarios when planning;
- Embrace new technology – use online planning tools, and seek professional advice.

Looking at retirement planning, ASFA, the Association of Superannuation Funds of Australia, have recently released their March 2017 Quarter Retirement Standard figures, setting out the amount required to live a modest and a comfortable retirement lifestyle.

These figures s reveal that the costs of a modest retirement for both singles and couples have risen by around a third in the past decade. Between June 2006 and March 2017, the ASFA standard for a modest retirement increased 33% for a single person and 36% for a couple, whilst the cost of a comfortable retirement rose by 23% for a single person and 26% for a couple.

During the same period, electricity costs jumped by 124%, health costs 60%, property rates and charges 83%, and food rose by 24%, meanwhile costs for clothing fell by 3% and telephone and mobile phone charges fell by 8%.

The March 2017 Quarter Retirement Standard budgets are:

	Couple		Single (Female)	
	Comfortable	Modest	Comfortable	Modest
Weekly	$1,150.13	$668.45	$837.41	$465.07
Annual	$59,971	$34,855	$43,665	$24,250

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Cost of Retirement

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Adjusting Retirement Expectations

In addition to seeking some really good financial advice from a financial planner, some useful pre-retirement suggestions include:

1. Understand exactly how much it will cost you to live in retirement – prepare a realistic budget, and account for emergency contingencies.

2. Consider deferring retirement – even if it means continuing to work on a part-time basis for a while.

3. Understand all the government benefits you are entitled to.

It is important to work out a realistic budget for your intended retirement lifestyle, remembering that many things will actually cost more than expected. It is also a great idea to consider practising living on your retirement budget before you actually retire.

If you are heading towards retirement, give your 'retirement budget' a trial run for a year. If you find that you cannot live on your planned budget, then you can either rethink your budget, rethink your planned retirement date, or assess the feasibility of continuing to do some paid work in retirement, to stretch those retirement dollars.

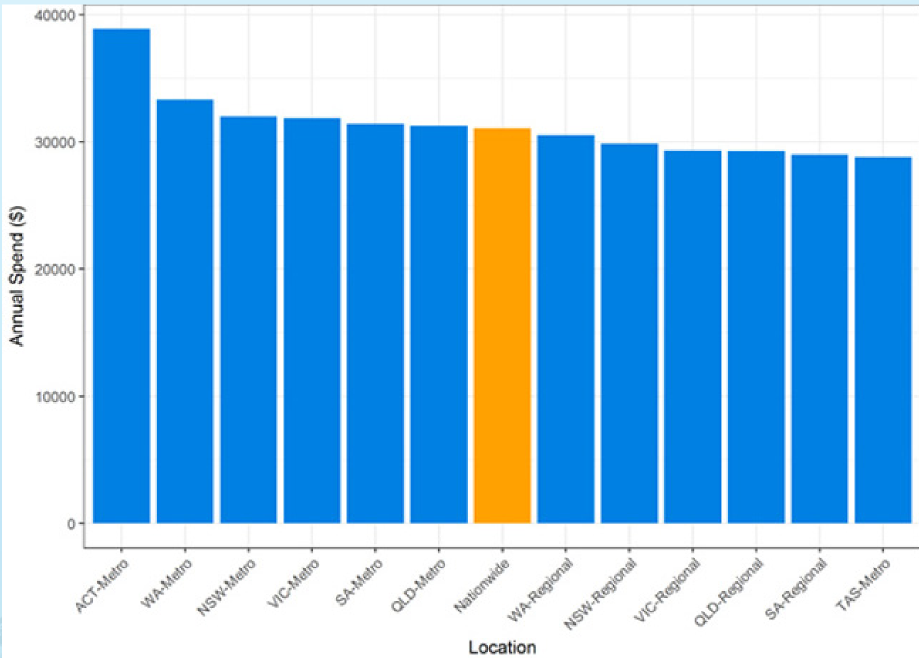
As was highlighted in the HSBC report, starting to save earlier, and saving more, will be the secret to being best placed to enjoy the type of retirement you have always dreamed of.

Retirement may be a journey rather than a destination, but the cost of the ticket varies widely depending on where older Australians live.

Where the median 65-69-year-old retiree lives can affect their annual spend by more than $10,000 a year according to the Q1 2017 Milliman Retirement Expectations and Spending Profiles report. The data, which analysed the real-world spending patterns of 300,000-plus retirees, shows that Canberra retirees have the highest annual spend of any region in Australia at $38,923 while Tasmanian metro retirees spend the least at $28,816, with the median spend across Australia at $31,068.

These differences reflect a general trend: retired Australians living in capital cities spend far more than those in regional Australia. Several factors could be driving this, including higher costs of living and higher incomes leading to larger retirement savings that support better lifestyles.

Figure 1: Median annual spend by location



Source: Milliman Retirement Expectations and Spending Profiles Q1 2017

- Depends on Where You Live

These expenditure variations create significant differences in target super balances. To fund the median annual expenditure of $31,068 throughout retirement with 75% certainty would require a balance of $129,621, assuming an investment in a balanced fund. This is not a simplistic target: it is based on stochastic modelling assessing thousands of scenarios incorporating the interactions of asset returns and inflation, spending drawdowns and the current Government Age Pension.

A Canberra resident would need a far higher balance, $280,444 at retirement, to fund their greater median annual spend of $38,923 with the same level of confidence. That's more than twice as much super, although the Age Pension would still provide two-thirds of expenditure over the course of retirement.

By contrast, a Tasmanian metro resident would need a super balance of just $91,829 to fund their much lower median annual spend of $28,816. The Age Pension (a maximum of $20,745 a year not including the Energy Supplement) would underpin the bulk of this expenditure (91%) over the course of retirement.

Figure 2: Breakdown by locations – Age 65

Source: Milliman Retirement Expectations and Spending Profiles Q1 2017

The variation in the super balance required at age 65 is almost $190,000 depending on a retiree's location. Australians will need to save more (or less) for retirement depending on where they live. A deeper analysis shows that where you live (and plan on retiring) plays a huge role and should form part of the retirement discussion.

Based on article by Jeff Gebler and Wade Matterson

Housing affordability:
Not just a problem for the young

"When you consider the increase in renting costs, it highlights the need for increasing numbers of retirees to have much greater super balances to support a reasonable retirement."

Sydney-based retirees who rent privately may have to save more than four times the amount of superannuation if they expect to live the same lifestyle as homeowners who own their homes outright, according to the Q1 2017 Milliman Retirement Expectations and Spending Profiles report.

It raises a new aspect to the housing affordability debate as skyrocketing property prices squeeze a generation out of the home ownership market.

The median retired Sydney homeowner aged 65-69 spends $31,987 a year, with the Age Pension (which is not affected by the value of the family home) funding the bulk of expenditure. Older Sydney residents stuck in the private rental market are not so fortunate. They must find an additional $21,679 a year, based on CoreLogic median estimates net of Centrelink Rent Assistance. This makes their annual cost of living two-thirds higher to fund the same quality of life enjoyed by homeowners. While Sydney has the highest rental costs, other capital cities show similar trends.

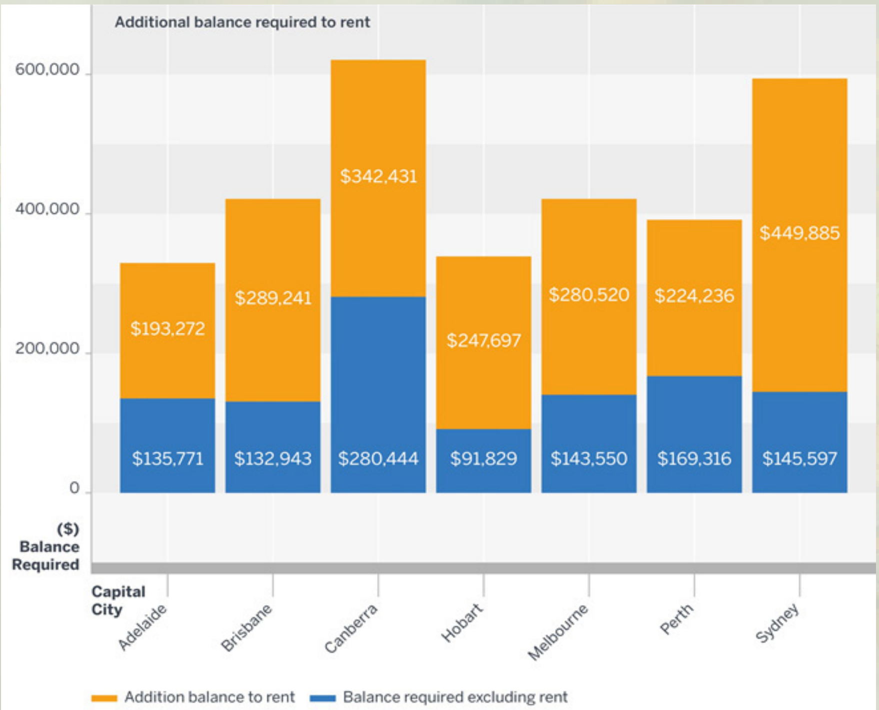
Figure 1: Median annual spend including rent payments 65-69yo

Source: Milliman Retirement Expectations and Spending Profiles Q1 2017

These differences in annual expenditure have even more significant repercussions for the level of super savings needed at retirement. To fund the median Sydney homeowner's annual expenditure through retirement with 75% certainty requires a balance of just $145,597 (largely because of Age Pension support). However, to fund non-homeowners' much higher annual expenditure through retirement with the same certainty would require a super balance more than three times that, at $595,482.

These forecasts are based on Milliman's sophisticated stochastic modelling assessing thousands of scenarios across a balanced investment option including variations in returns, inflation, spending drawdowns and the impact of the Age Pension.

Figure 2: Superannuation balance required to rent (75% certainty)



Source: Milliman Retirement Expectations and Spending Profiles Q1 2017

Whilst these issues currently only affect a small number of retirees, the problem is likely to increase in the future, given that the level of home ownership is dropping across all other age groups.

Around three-quarters of older Australians are homeowners while 7.3% live in private rentals, according to the December 2015 Productivity Commission report. However, the Household, Income and Labour Dynamics in Australia (HILDA) Survey shows home ownership levels for people aged 35–44 dropped from 63.2% to 52.4% between 2002 and 2014. Similarly, home ownership levels among people aged 45–54 declined from 75.6% to 67.4% over the same period.

Australian residential property, led by Sydney and Melbourne, now ranks among the most expensive in the world. Since June 2012, residential property prices across Australia's capital cities have climbed by a cumulative 47.3% with Sydney prices up 74.9%, according to CoreLogic.

Outright home ownership has traditionally been seen as key to avoiding poverty in old age. However, as housing affordability edges further out of reach, this could lead to a greater proportion of older Australians paying off their homes well into retirement.

This new data shows that rising property prices are a problem we're not growing out of with age.

Based on article by Jeff Gebler and Wade Matterson

Australia,
A Fast Changing Nation

The Census has helped update Australia's estimated resident population, which has grown to 24.4 million people by December 31, 2016.

The first snapshot results of the 2016 Census released by the Australian Bureau of Statistics, paint a picture of a rapidly changing nation and marketplace.

The 2016 Census counted 23,717,421 people in Australia on Census night, which included 23,401,892 people who usually live in Australia – an 8.8 per cent increase from 2011. On Census night, over 600,000 Australians were travelling overseas.

Population growth is increasing. In the 40 years between 1966 and 2006 Australia's population grew 1.4% each year, but in the last decade this growth rate jumped by 20% to 1.7% each year.

This population growth is driven by fertility, longevity and immigration - and it is resulting in a nation that is ageing as Australia's median age has jumped from 36 to 38 years.

Reflecting this change, the proportion of people aged 65 or older has increased from 14% to 16% of the population. The 2016 Census found that there are 664,473 additional people aged 65 and over since 2011. Tasmania is our most experienced state, with nearly one in five people aged 65 and over. The Apple Isle also recorded Australia's highest median age (42 years), ahead of South Australia (40 years).

More older Australians also means more older women. Across the population, 51% are female, and among Australians aged 65 plus the proportion of women jumps to 54%. Among Australians aged 85 plus the proportion of women rockets to 63%.

The implications for aged care planning, household structures and retirement income product designs will be significant.

Australia's population doubled in the past 50 years, and is likely to double again in the next 50 years, to about 50 million, 80% of whom will probably live in urban and capital cities. This also comes with huge infrastructure development needs - and investment opportunities.

It is predicted that Australia's centre of gravity will shift south towards Melbourne, away from Sydney. Greater Melbourne with a population of 4,485,211 is growing 12% faster than Greater Sydney with a population of 4,823,991, with Melbourne gaining 1,859 people every week compared to Sydney's 1,656 since the 2011 Census.

Yet it's the home of the nation's capital – the Australian Capital Territory (ACT) – that experienced the largest population growth of any state or territory over the past five years, adding more than 40,000 new residents – an increase of 11 per cent.

But while the population is going up and concentrating in Capital cities, the proportion of households in Australia renting their accommodation has climbed from 27% in 2011 to 31% in 2016, a change that will only exacerbate concerns about Australia's residential property market and housing affordability.

However, this may explain why apartments, flats and townhouses have increased as a share of all housing dwellings from 24% to 27% over the past decade.

The Australians who will live in these dwelling will be more culturally diverse. Fifty years ago in 1966 just 18% of Australians were overseas-born, today this ratio is 26%. In 1966 one third of these people were born in England but today this share has plummeted to 15%. The proportion from New Zealand also decreased over the same period from 9.1% to 8.4%.

The proportion of overseas-born Australians born in China has meanwhile jumped from 6% to 8.3% and the proportion from India has jumped from 5.6% to 7.4%. The Philippines accounts for 3.8% of overseas-born Australia, up from 2.7% at the 2011 census.

This pace of change in Australia's cultural diversity is dwarfed by Australia's changing religious affiliations. In 1966 almost nine in 10 Australians reported a Christian faith but in 2016 this ratio has plummeted to just one in two. The 36 percentage point change was mostly offset by the 30 percentage point increase in the number reporting no religious affiliation.

As reported in the Financial Standard and ABS Media Release from 2016 Census

Small Money Moves Can Have a Big Impact

When it comes to money, small changes may work better than big ones. There is a saying if you watch the cents the dollars will follow. It's because smaller bite-size changes are more likely to grow into new habits that stick. Try these small money moves to build habits that can have a major impact on your financial success.

1. Save a Little

Sure, saving a lot would be great. But saving what you can is even better. Maybe that's $10 a month into the piggy bank on the kitchen counter, putting an extra $25 a month into your bank savings account, or adding a regular contribution to your superannuation.

Small moves like this have a big impact over time.

2. Make an Extra Payment

What if you made one extra mortgage payment a year? Or rounded your car payment up to the nearest hundred dollars? A little extra here and there can mean your mortgage is paid off years in advance or your car is paid off months in advance.

Depending on your mortgage loan you may have to make the entire extra payment at once rather than paying a little more each month. If you add a little extra each month the lender may not apply the extra payment to principal. Contact your lender to find out how to pay extra in a way that the excess payment reduces your principal balance.

3. Read a Finance Book

A single book can impart knowledge that will serve you for a lifetime. Even if you don't like reading, surely you can get through one book? One great book is Behavior Gap, by Carl Richards, on how our behaviours cause us to unknowingly make unwise decisions with our money.

4. Organise

Financial stuff can feel overwhelming. A simple step you can use to make it more manageable is to get your financial information organised.

You need to know where you are currently in order to work out how to get where you want to go, and the best way to do this is to be organised!

5. Buy Used

Cars, furniture, clothing… you can almost always find what you want and pay less for it by buying used. If you get into the habit of looking for used items first you can save hundreds, sometimes thousands, each year.

6. Cancel Something

Too many of people some type of recurring charge that is coming out of your bank account or being charged to your credit card for something you don't even use. It might be a magazine subscription, annual membership fee, or something you signed up for accidentally. Scour your statements and make time to cancel those things you don't use.

7. Turn Off Financial TV

One client told me that one of the things he really liked about working with a financial planner was that he didn't watch financial TV anymore.

He found life to be far more relaxing once he tuned that stuff out. Everyone can benefit from turning off the financial stock tip shows. Put a solid long-term plan in place and watch stuff that will make you laugh - not stuff that will only stress you out.

Inspired by Dana Anspach

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