PROFESSIONAL PLANNER

INSPIRING ADVICE

ISSUE 72 » FEBRUARY 2015

PLUS

STEP-BY-STEP GUIDE
Everything accountants must know about licensing options

BRACE YOURSELF
Is the end of the equity yield play nigh?

RETIREMENT PLANNING *KICKS THE BUCKET*

How new thinking is reshaping strategies and portfolio construction

GRANT MCCORQUODALE, HEAD OF PRIVATE CLIENTS AND INTERMEDIARIES, FIIG

Direct fix for bond investors

Better access to direct bonds will make it easier for retail investors to include the appropriate amount of fixed-income investments in their retirement portfolios. Glenn Freeman reports.

The rising life expectancy of Australians and the rapid growth in self-managed super funds (SMSFs) are fuelling a resurgent interest in fixed-income investment for financial planners and their clients.

As a key defensive asset class, bonds are particularly important for investors requiring a reliable income stream and stable growth.

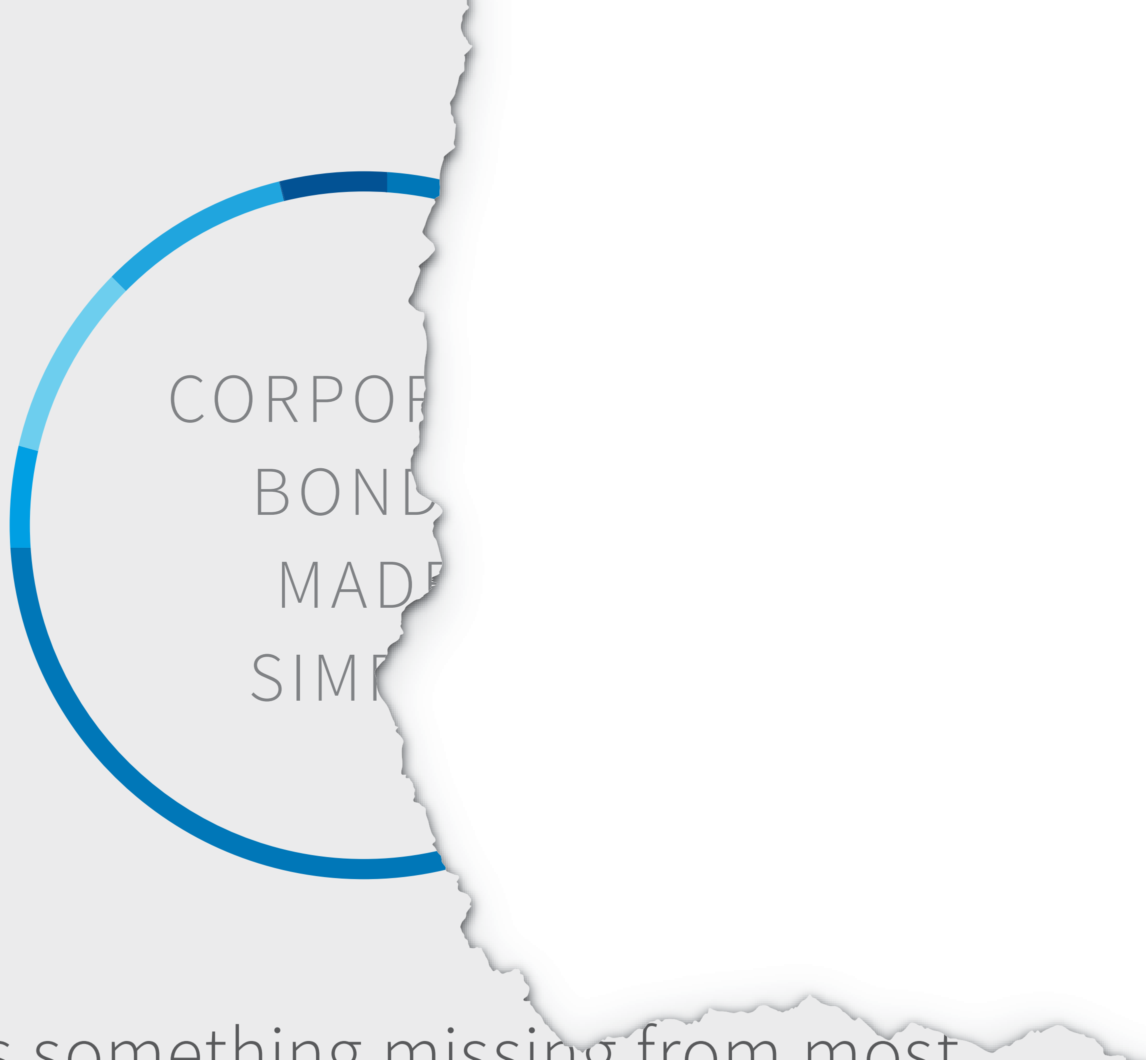
"They're looking at the risk of their capital and saying, 'it needs to last the distance'," says Grant McCorquodale, head of private clients and intermediaries, FIIG.

"This is where I see the retirement income policy landscape in Australia, because in one generation, you've got people living 14 years longer."

He refers to data that shows average life expectancy in 1970 was 71 years; "now it's 85, and in 10 years it will be 90. It means people need to ensure their money lasts the distance".

McCorquodale sees strong outflows of cash from term deposits into the equity markets as retirees attempt to boost capital growth and ensure their money lasts long enough.

"While the markets were correcting themselves strongly, every client said 'show me the cash flows, reassure me they're robust because that is what I need to live on each day'.



There's something missing from most Australian investment portfolios.

It's bonds.

The world's leading investment managers invest around 25% of their pension assets in bonds, yet in Australia the typical SMSF trustee has less than 5% of their assets in bonds.*

If you're approaching retirement or already retired, you should be thinking about bonds. Bonds diversify your portfolio, offer regular income with rates from 4% p.a. to 8% p.a. and protect your capital.

To find out more, visit **fiig.com.au/professionals** or call 1300 752 663.

Winner Fixed Income, CoreData Service Provider Awards 2013 & 2014

*Source: Mercer, Asset Allocation of Pension Funds Around the World, February 2014

FIIG-PORTFOLIO-PRO-PLN-1

FIIG | The fixed income experts

fiig.com.au | 1300 752 663

FIIG Securities Limited ABN 68 085 661 632 AFS Licence No. 224659
FIIG provides general financial product advice only. For a copy of our disclaimer please refer to *fiig.com.au/disclaimer* A corporate bond is not a bank deposit. Corporate bonds have a greater risk of loss of some or all of an investor's capital compared to bank deposits. Unless specified otherwise, figures provided as at 27th January 2015 and subject to change.

THIS IS WHERE I SEE THE RETIREMENT INCOME POLICY LANDSCAPE IN AUSTRALIA, BECAUSE IN ONE GENERATION, YOU'VE GOT PEOPLE LIVING 14 YEARS LONGER

"People have an income line and an expense line…the income line needs to be more robust than their anticipated expenses. It's an important question for SMSF trustees, to make sure they've got exposure to the fixed income market, to make sure they've got certainty around their income streams.

"What they really want is bonds, but they're getting equities," he says, pointing to a lack of understanding of fixed income, combined with limited direct access to fixed-income markets for retail investors.

He says FIIG opened up corporate bonds to private investors in 2010, when it began purchasing institutionally-sized parcels of the bonds and repackaging them into $10,000-sized portions, subject to a $50,000 minimum spend.

"That's what really opened up the bond market to SMSF and private investors," McCorquodale says.

Last year, FIIG doubled its client base, and this year expects about 50 per cent growth in new clients.

"It really is a market where the trustees want the bonds, but previously haven't had a market to access them directly," he adds.

"The biggest risk that Australians face is less [in] market risk, and more in longevity risk," McCorquodale says. "Now we need super money to last 25 years, and now people in their 30s and 40s will need it to last 30 years [when they retire]. That's where global pension funds have understood the actuarial risks of capital depreciation."

He believes many SMSF trustees do not understand how to go about selecting the most appropriate asset mix.

FINANCIAL PLANNERS AND BONDS

To better facilitate clients' access to fixed-income products, financial planners need more seamless, ready access. Traditionally, direct bonds are not traded via stock exchanges, but primarily through over-the-counter trades.

This is a key difficulty alluded to by David Middleton, a director of Adelaide-based financial planning business, Middletons Securities.

"We've found the process of accessing them a bit clunky, a bit opaque," he says. Despite this, in recent years Middletons has increasingly been making bonds available to its clients.

"We've been very interested in some of the index bonds, because they've been very cheap, [with] running yields of 3.4 per cent. You were essentially getting the inflation protection for nothing," Middleton says.

Because of the difficulties in having to buy bonds over the counter, Middleton says he would welcome online access to purchasing fixed-income products.

FIIG intends to roll this out very soon, when it launches what McCorquodale believes will be the first online ordering system for direct bonds.

"At the moment, our clients come in and speak to our bond dealers and discuss the options and each of the individual securities," he says.

However, once FIIG's new service is launched, this should provide a platform allowing advisers or private investors to go online, make their own self-assessment and submit trades online.

"This is the next stage in opening up the bond market to private investors. Clients will still need to speak to our dealers to understand the nuances, but it's certainly the platform that opens up much more transparency around supply and market pricing," McCorquodale says.

VIEW FROM THE ASX

A general lack of understanding of the bond market is a key constraint on greater expansion of the market, according to Ken Chapman, head of debt capital markets at the Australian Securities Exchange (ASX).

He believes that to be providing the best advice, there is an imperative for financial planners to understand fixed-income products in the same way they need to understand equities.

He also says that they need to be able to access the market – not only to see prices, but to obtain detailed, timely credit reports.

"They need to be able to access fundamental data about the issuer, to see where the particular debt instrument sits in the credit structure," Chapman says.

In this sense, he believes the ASX partnership with Australia Ratings provides a useful service. Launched towards the end of last year, this service assigns credit ratings to all debt products.

"So now financial planners can go to Australia Ratings and get the information on a particular security's credit rating, and get a report on the product's complexity. It's important to understand not just the credit rating of the issuer, but also the complexity," Chapman says.

A PSYCHOLOGICAL SHIFT

Having held senior roles inside the advice businesses of Macquarie and JBWere, before joining FIIG, McCorquodale has observed a "binary shift" in asset allocation when investors transition from the accumulation phase to the retirement phase.

"That's a major reflection going on in someone's life, and how it translates when it comes to investing," he says. "People are very comfortable taking 70 per cent growth and 30 per cent balanced assets when they're working, because if they get it wrong, they can repair their losses.

"However, I've seen [that] the psychology shifts significantly when they retire, because there's no future cash flow to repair their losses; their willingness to take risks stops," he says.

McCorquodale describes this as a resetting of their asset allocation models, when their growth/defensive exposure often shifts from 70/30 to something more like 30/70. P