The Retirement Advice Centre

August 2015

Are we there yet? That's the question on everyone's mind as August begins and we enter the final sprint towards spring and warmer weather. Winter in Australia is all about sport, and we've been spoiled for choice this winter with tennis, cricket, cycling and plenty of action on the football field. But some of the biggest action has been on investment markets.

July began with the ongoing Greek debt crisis, but that was soon overshadowed by the wild ride on the Chinese sharemarket. Up 150 per cent in the year to June, the Shanghai Composite fell 30 per cent by early July, rebounded then fell again late in the month. While Chinese share prices are still higher than they were at the start of the year, the volatility has un-nerved investors. Australian shares tossed and turned with the big miners – already weakened by falling commodity prices – especially hard hit. The Australian dollar dipped to a new six-year low of US72.57c before settling just above US73c.

Parts of the local residential property market continued to sizzle, despite the cold. The median Sydney house price jumped the psychological hurdle of $1 million in July. Australian consumers also showed renewed confidence. After sliding by eight per cent in the first two weeks of July, the ANZ/Roy Morgan consumer confidence rating lifted by more than 5 per cent in the final fortnight.

Chinese dragon mauled by bears

In the space of a generation China has gone from economic backwater to global heavyweight. But as its stellar growth begins to slow, the Chinese government has been trying to finesse the transition from a construction-based economy to one based on domestic demand. Part of that strategy involved talking up Chinese-listed shares.

Wealthy Chinese households responded by borrowing to the hilt and piling into shares – until June, when the bubble popped and panicked investors rushed for the exits. After climbing 150 per cent in the year to June 12, the Shanghai Composite Index fell 30 per cent in under four weeks.[i]

Prices have rallied and fallen again since then, but only after some extraordinary intervention by the Chinese government. New listings were suspended, more than 1300 companies were put in a trading halt and the central bank gave additional funds to stock brokers so they could extend margin loans to clients.[ii]

What just happened?

The Chinese sharemarket's recent tremor sent shockwaves through global investment markets already nervous about a possible Greek exit from the Eurozone. Which begs the question – what just happened in China and does it matter to Australian investors?

This latest bubble is not the first, or the worst, for the fledgling Shanghai stock exchange. However, the latest surge was different to the last because it was not supported by economic growth.

China's economic growth has been slowing from double-digits at the height of the boom to a six-year low of 7 per cent in the June quarter.[iii] This latest figure was better than feared though, which should

boost investor confidence in China and abroad.

Debt levels soar

The defining attribute of this latest sharemarket crash is the number of newly-minted shareholders armed with margin loans. More than 40 million stock market accounts were opened between June 2014 and May 2015, taking the total number of trading accounts to 90 million.[iv]

When you add debt to the mix, share price rises and falls are bound to be magnified. By June this year, Chinese investors had bought US$350 billion worth of stocks with borrowed money. And it's not just individuals gambling with margin loans.[iv]

Chinese listed companies have been using their own stock as collateral for bank loans to bet on the sharemarket or commodities. This means they were hit with margin calls even as their share prices and the broader market fell.

The fallout for Australia

As China's share bubble popped, iron ore price fell more than 30 per cent in a fortnight to a six-year low of less than US$45 a tonne. One reason for this was that commodities are often used as collateral for bank loans and investors were forced to sell commodities to meet margin calls on their shares.[v]

Another reason for iron ore's heavy falls is the slowdown in the Chinese property market as it digests an oversupply of apartments. Residential construction is a major consumer of Australian steel.

Australia's iron ore majors, BHP Billiton, Rio Tinto and Fortescue Metals Group all suffered heavy share price falls in the four weeks to mid-July but have since recouped some of their losses.

The dollar

Global market instability is behind an influx of capital into safe haven assets such as US bonds, pushing up the value of the greenback. In the wake of the Chinese market crash, the Australian dollar fell below US73c for the first time in six years.

China's rapid rise from developing to developed nation and more open markets is bound to have some hiccups along the way. What this latest market meltdown exposed is the need for further economic reforms. It also serves as a reminder that what is good for China's economic development is good for Australia and Australian investors.

If you would like to discuss the issues raised in this article in the context of your portfolio, please give us a call.

i "China's stock bubble burst' by Anthony Fensom, Morningstar 10 July 2015.
ii 'Whiplashing week takes world markets for a riotous ride' by Vanessa Desloires, Sydney Morning Herald, July 11-12 2015, page 8.

iii CommSec Economic Insights, July 15 2015
iv Vox http://www.vox.com/2015/7/8/8911519/china-stock-market-charts
v 'Dr Copper calls double trouble' by Karen Maley, AFR 11-12 July, page 34.

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Starting over: divorce after 50

Baby boomers have always been catalysts for social change and now they are doing it again. Divorce after 50 – or grey divorce as it's become known – is on the rise. At a time when the kids have left home and retirement is on the horizon, more couples are deciding to go their separate ways.

While the overall divorce rate has fallen slightly in recent years, empty nesters are bucking the trend. That's pushed up the median age of divorce to 45 for men and 42 for women, from 38 and 35 respectively back in 1990.[i]

After decades of building up assets, divorce can create special challenges for people near the end of their working life. But with careful planning it is possible to achieve a positive outcome, both personally and financially.

Do your sums

The first step is to do a realistic inventory of your marital assets and liabilities. That will enable you to make informed choices about the best way to split your finances to achieve long-term financial security.

You will also need to draw up a budget. This is especially the case if one of you had little to do with

the household finances and investments while you were married. Suddenly you are contemplating a new lifestyle with different financial responsibilities so it's important to work out how much income you can count on and what your cost of living will be.

At this point it is a good idea to talk to your financial adviser. They can help develop a financial plan that will allow you to achieve your immediate and long-term lifestyle preferences.

For some people, it may be necessary to continue working for a few years longer to stretch your retirement savings further. One or both partners may need to re-enter the workforce, take on part-time work or update skills.

Think long-term

It's common for people to have an emotional attachment to their family home, but keeping it as part of the divorce settlement may not necessarily provide the best financial outcome. Large homes and gardens can be expensive and time-consuming to maintain.

Think about how and where you want to live now and into the future. If you hold on to the house, do you risk being asset rich and income poor in retirement?

If you sell the house, could you downsize and release some extra cash for living expenses or to invest in super?

Take tax into account

It's also important for divorcing couples to take into account the tax implications of dividing superannuation, selling a business or divesting from investments.

In the heat of divorce proceedings it's often tempting to forgo super in exchange for the family home or more liquid assets. But super is such a tax effective investment vehicle, it makes sense to hold onto your entitlements if at all possible and start rebuilding your balance with salary sacrifice or personal contributions.

Review insurance

Now you are single, it's time to review your insurance cover. Policies held in joint names should be revisited.[ii] And if you are still working and paying a mortgage or rent it is wise to consider income protection.

Life insurance policies where your ex remains the beneficiary should you die may no longer reflect your wishes. You will probably also want to write your former partner out as a beneficiary of your super and close all joint bank accounts.

You also need to update your will and estate plan to protect your children's inheritance. Many people don't realise that an existing will does not automatically become invalid on divorce.

If you plan to re-partner, consider a prenuptial agreement – officially called a 'binding financial

agreement' – drawn up by, and signed in the presence of, your lawyer. This may help prevent family disagreements and costly legal disputes later on.

Divorce is never easy, but with careful planning it can open up new opportunities for personal happiness and growth.

i http://www.abs.gov.au/ausstats/abs@.nsf/mf/3310.0
ii https://www.moneysmart.gov.au/life-events-and-you/life-events/divorce-or-separation#organising

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Take a day: it can pay

Ever thought about taking a break from your routine, a "Financial Health Day" to spend some time tightening up your personal finances?

While it might not be the most exciting day you will ever spend — unless the thought of saving a significant amount of money excites you, it will be worth your while.

It should be a weekday so you have scope to call banks, credit card issuers, health insurers, and other financial service providers who are easier to contact during office hours. And you will also need all your tools — financial records, current tax return, mortgage, credit card and bank statements — close at hand. Internet access is also important as there are many things you can do online.

Hitting the target

So, what are your objectives? Well, there are two sides to this coin. The first objective is to put more $$ in your pocket by saving a little more and spending a little less of your income, without making

your life a penny-pinching misery in the process. The second is to discover some cheaper ways, if they exist, to pay for some of life's essentials.

Start at the beginning by reviewing your monthly budget — or constructing one, if necessary — so you can pinpoint the big expenses before trying to pare them back. Take your power bills, for example. Some power companies will not only reward you with a discount for combining your gas and electricity, they will also allow you to pay them with a pre-set monthly direct debit, avoiding the shock of that big quarterly hit and smoothing your cash flow.

Monthly payments or saving targets can be an excellent budgeting tactic. In fact, you can even create your own monthly debit system for major expenses such as school fees, annual holidays and Christmas by estimating the cost and transferring monthly instalments to a separate savings account. Your bank can probably make the transfers for you automatically.

If you can manage it painlessly by cutting one or two unnecessary expenses, one good outcome of a budget review would be to save an extra 1 per cent of your salary — just $1 out of every $100 you earn — for a major objective like an overseas trip, new carpets or as a reserve fund. The best budgets can be wrecked by unexpected emergencies, whether it is a burst water heater or an unexpected mortgage rise.

Smart moves

Once you have your budget review completed and have set up new direct debits and/or opened one or two new dedicated savings accounts, you should still have a few hours of your Financial Health Day left to look for some significant savings on financial services.

Credit cards are a black hole in many budgets. Could you save by switching to a cheaper card? Are you paying off your card within the interest-free period? What about rewards programs — if you are paying for them, are you using them? Some supermarket reward programs now offer a "double reward" so it may pay to investigate your options. You can compare cards online at several sites such as www.creditcards.com.[i] And if you do decide to change card companies, you might find one that will give you an interest rate holiday for the first 3–6 months as a reward for switching.

Your private health insurance plan is also worth reviewing because your family circumstances might have changed since you took out the plan, or the market may have newer, more flexible options. A Choice Magazine report on 40 private health funds may be a good starting point if you are looking for better value, since they reported cost differences of up to $800 a year or more. (See www.choice.com.au[ii] or www.privatehealth.gov.au)

Planning ahead

And finally, if you haven't had an annual check-up, make time before the end of the day to contact your adviser and arrange to review your superannuation and investments, to ensure your financial planning strategy is still on track.

All done? Congratulations on a good day's work!

i http://www.creditcards.com.au/compare/
ii http://search.choice.com.au/consumer/Health%20Funds

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