# THE GENERATOR

*An investment in knowledge pays the best interest – Benjamin Franklin.*

Q1/21


# RETIREMENT KILLERS TO AVOID AT ALL COSTS

FINANCIAL PLANNERS SEE PEOPLE MAKING THESE SIX MONEY MISTAKES ALL THE TIME, AND THEY CAN ENDANGER YOUR RETIREMENT.

Six retirement killers, and remedies to get back on track.

1. **Not having a written income plan.**
   Many retirees are winging it, without a plan that tells them how much they will need from year to year, or even worse, how long their money will last.
   **The remedy:** An income plan is like a compass. You'll always know where you are, and where you're going.
2. **Using the wrong investment return assumptions in your income plan.**
   If you're counting on a 9% return to make your plan work, for example, and the market doesn't cooperate, you will most assuredly run into trouble!
   **The remedy:** Be a bit conservative when making assumptions about market performance. Your income plan should use a withdrawal rate of no more than 4% to provide income, and be sure that your portfolio is positioned to avoid wild swings in the market.
   Keep 18 months to two years in cash available so you are not forced to sell when the market value is down.
   Cash and more stable investments help you get through a bear market.
3. **Taking too much risk with investments.**
   Some people get so caught up in accumulating money they forget to protect what they have in or near retirement. Others mistakenly think they have a moderate or conservative portfolio when what they actually have is quite aggressive. →


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## THE MONTH AHEAD

International equity markets were mostly higher in March, as cyclical and value stocks pushed some indices to new all-time highs. In the US, the S&P 500 and Dow Jones Industrial Average both traded to all-time highs, and with a few days left in the month were up around 4%.

Many European markets were on track to post solid gains for the month, while in New Zealand, the NZX 50 was on track to finish the month higher, but continued to under perform most global counterparts.

The rally came amid further optimism on the global growth outlook as economies →

*Inside*

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**The remedy:** A financial adviser can do an exhaustive review of your investments, simulate how they would react to historic market crises, and assess how vulnerable your current portfolio might be to future corrections.

4. **Not enjoying the people and activities you care about.** Some retirees are so uncomfortable with seeing the balance of their retirement account go down that they spend less than they can afford – not taking the trips they once dreamed of or visiting their grandkids as often as they could. Then, 20 years into retirement, they turn 85 and realize as time has ticked away, they haven't done a thing.
**The remedy:** The goal here is to find a happy middle ground, and a "bucket" strategy for your assets can give cautious retirees confidence to enjoy their money. In this approach, each bucket provides for a different need – you might have a 'safety' bucket for money you can get your hands on any time (cash and cash equivalents) to use for vacations and big purchases. An 'income' bucket includes assets that are reliable and protected from the market e.g. superannuation that you can use to pay your bills. And a 'growth' bucket holds riskier assets that are chosen to build wealth for future needs and to counter inflation.

5. **Giving too much money to the kids.** I have seen this retirement killer in many forms: parents with grown children who still depend on them for everyday living expenses, and others who are paying off their children's student loans. Some parents loan their kids money at low/no interest, or agree to co-sign on a loan or mortgage. Parents may gift money to their children too soon and then come up short on what they need for themselves early or later in retirement.
**The remedy:** When you fly, they always tell you to put your oxygen mask on first, before you help the person next to you. That should be a rule for parents when it comes to gifting or lending money to their children. Always make sure you are okay first, and if that makes you feel stingy, think of it this way: you're giving your kids a different kind of gift – the gift of financial independence, for them and yourselves, too.

6. **Blindly believing when your financial professional says, "You are going to be okay."** If you don't have a plan, or you don't understand your plan, you aren't okay, no matter what your adviser says.
**The remedy:** If you're paying for advice, you should be getting it. If your financial professional can't make time to build a plan for you or doesn't have the ability to do so, you should be concerned. Or, if he or she is focused primarily on growth vs conservation and income, it may be time to move on.

## *Life's tips/1*

"Successful investing is about managing risk, not avoiding it."
*– Benjamin Graham.*

***A good plan can help you overcome bad choices – the sooner you get back on track, the better you'll feel.***

*'Month ahead' continued from page 1.*

continue to reopen, albeit cautiously.

As we head into April, Biden's infrastructure plan will unfold, and central bank meetings highlight the calendar.

**Prominent central banks have their own specific issues**

A number of central banks are set to meet.

A decline in 2020 fourth-quarter GDP and uncertainty around the housing market means we think there is a slightly higher chance the The Reserve Bank of New Zealand will cut the Official Cash Rate from 0.25%.

The US Federal Reserve is likely to leave its cash rate unchanged. With a robust COVID-19 vaccination rollout underway, massive fiscal stimulus supporting the economy and the prospect for some pent-up spending, the Fed will have to manage market expectations for changes to monetary policy settings, to avoid any disorderly behavior in the bond market.

Any spike in yields would increase borrowing costs and potentially dampen the recovery. The Fed has reiterating the need to see inflation remain above 2% for an extended period, and see recovery in employment before reducing monetary policy support.

The European Central Bank conundrum is a worsening COVID-19 situation which has led the ECB to increase the pace of their Asset Purchase programme. This could see the central bank put pressure on governments to enact fiscal support.

**Fiscal and tax policy a significant driver**

As bond market volatility has subsided, our focus has shifted to pending changes to fiscal and tax policy. After passing the US$1.9 trillion COVID relief bill, Joe Biden has turned to infrastructure and will unveil his infrastructure package expected to cost around US$3 trillion.

**Optimistic on the economic outlook**

Our positions remains that we are overweight international equities, Australian equities and real assets. The US vaccination rollout is likely to result in some strong economic figures for the middle and latter parts of 2021. In fixed interest, we remain underweight both domestic and international bonds. With inflation expectations continuing to rise amid an improving economic outlook, we have seen a move higher in long-dated yields benefiting these positions. While central banks remain accommodative, the outlook for further rate cuts in developed markets has diminished.



## *Summing up*

••• Being careful about your money means being careful with what you believe.
••• Global financial outlook getting a jab in the arm?

# FOUR THINGS EVERYONE NEEDS TO KNOW ABOUT *THE MARKETS*

ONE OF MY FAVORITE ANNUAL MARKETS UPDATES COMES FROM THE CREDIT SUISSE GLOBAL INVESTMENT RETURNS YEARBOOK BY ELROY DIMSON, PAUL MARSH AND MIKE STAUNTON.

Every year it provides valuable insights or useful reminders about the importance of a long-term mind-set in the financial markets.

These reminders are more important than ever in a society that focuses more on the day-to-day or even minute-to-minute when it comes to the markets. Here are four reminders from this year's update:

1. **Stocks beat bonds over the long-term.** Dimson, Marsh and Staunton give an update of the real returns by country for stocks, bonds and cash going back to 1900. In all 25 countries studied, stocks beat bonds and cash and by a considerable margin in most cases. And bonds have outperformed cash in every country but one. The results aren't equal across all countries. Some had negative real returns, which mostly came from war or hyperinflation in the first half of the 20th century. But over the long-term, there is a clear relationship between risk and reward. Stocks are riskier than bonds or cash in the short-run so they have higher returns in the long-run.
2. **The long-term doesn't matter if you can't survive the short-term.** Bonds and cash, while seemingly useless over the long-term, can be essential over the short-term. This is true for both practical and emotional purposes. The practical use of bonds and cash is having an asset that can be used to buy stocks when they're down or avoid selling your stocks when they're getting crushed. And the emotional use of bonds and cash is having an asset that can dampen volatility, both in your portfolio and in your emotions. Owning bonds can be a hedge against bad decisions at the worst possible time so you can make it to the long-term with your stocks.
3. **Inflation plays a bigger role than you think.** Inflation takes a huge bite out of everything. This is both the good and the bad of compounding. Over very long periods of time returns in stocks, bonds and even cash can lead to substantial growth. But inflation compounds against you as well. It's like an expense ratio that changes over time. Beyond your goals and dreams, this is the whole reason for taking risk in your portfolio in the first place. You have to if you wish to beat a rising standard of living.
4. **Markets are constantly changing.** The United States made up just 15% of global equity markets in 1900. Now it is close to 60%! Britain's share has shrunk by a factor of six. Germany and France have seen similar slippage. Then you have countries like Japan and China that weren't even in the market in 1900 but now have the second and third largest market share.

**Look at the railroads!**

I like to look at S&P 500 data going back to the 1920s but much of that data comes from a recreated index. The actual S&P 500 began in 1957.

The original S&P 500 consisted of 425 industrial stocks, 60 utilities, and 15 railroads. Financial stocks weren't added until the 1970s. Technology didn't really exist as a sector in 1900. Now it dominates the market. So while the stock market itself remains a great bet over the next 120 years or so I would never go out on a limb to predict what the winning country or sector will be in that time.

Will the U.S. continue to dominate? Or will emerging or frontier markets step in to take market share? Will tech hold its place as the king of the hill? Or will another sector grab the lead because of a shift we can't even see coming at the moment?

This is what makes markets so hard. The general relationship between risk and reward is fairly straightforward over the long-term.

***Picking the winners within the stock market will always be easier in the rearview mirror.***

## *Life's tips/2*

"The key is in not spending time, but in investing it."
– *Stephen Covey.*

*Summing up*

- Equities are still better than bonds and cash.
- Tech replaced tracks, but what will the future bring?

# WHY PEOPLE *WONT* CHANGE THEIR MINDS

WHEN FACED WITH THE PROSPECT OF ADMITTING YOU'RE WRONG OR LOOKING FOR A BETTER EXPLANATION, MOST PEOPLE GET BUSY LOOKING FOR AN EXPLANATION..

On December 17, 1954, The Chicago Tribune ran the following headline: '*Doctor warns of disasters in world Tuesday.*' The paper interviewed Dr Charles Laughead at the home of Dorothy Martin. Martin said that she had received messages "from outer space" that the world would be ravaged by a great flood that would end life on earth, save for a small group of disciples who were stationed at Martin's home. This group was so committed to the cause they sold their possessions, quit their jobs or stopped going to school in preparation.

The newspaper didn't put much faith in this prophecy, but Martin's followers were true believers in her word. As the group sat outside of Martin's home on D-Day – Christmas Eve – they sang and waited with anticipation for the coming of their saviors.

Their alien brethren failed to show.

At a loss for words, Martin finally garnered up the energy to talk. As luck would have it, the group had spread so much light that God had saved the world and there was no longer a need to exit the stage!

A few hours after their failed predictions, Dr Laughead said the following:

"I've had to go a long way. I've given up just about everything. I've cut every tie. I've burned every bridge. I've turned my back on the world. I can't afford to doubt. I have to believe. And there isn't any other truth."

The members could have chosen to look themselves in the mirror and realise their end of the world prediction was ridiculous but that would have required admitting the outlandish actions they took and beliefs they held leading up to that point were false.

The concept of cognitive dissonance was developed by psychologist Leon Festinger in the 1950s. It arises when a person holds two beliefs that are inconsistent with one another. The theory is that when this happens it causes our minds discomfort which we then seek to reduce. Whenever this inconsistency in our attitudes, ideas or opinions kicks in our default is to eliminate that dissonance.

Festinger's asked participants in a study to perform a series of boring tasks for an hour. When the tasks were completed they were to tell waiting subjects that what they were doing was very exciting to entice them to do the same. They were then paid either $1 or $20 for this acting performance.

The study found that those who were paid $1 rated their experience performing a dull task as being more enjoyable than the people who were paid $20. The $1 group talked themselves into it being enjoyable to reconcile the fact that they wasted time, earned little and lied to others about it. This dissonance was overcome by the false belief that what they did was more enjoyable than it actually was, while the people who were paid $20 were able to recognise they were simply doing it for the money. Basically, cognitive dissonance leads to self-delusion.

Festinger and a team of researchers heard about Martin and her followers and decided it would be the perfect real world study. They witnessed the group leading up to their end of the world prediction, and in the aftermath of the failed prediction as well. Festinger concluded: "A person with conviction is nearly impossible to reason with... Suppose an individual believes something with his whole heart; suppose further that he has a commitment to this belief, that he has taken irrevocable actions because of it; finally, suppose that he is presented with undeniable evidence, that his belief is wrong: what will happen? The individual will frequently emerge, not only unshaken, but even more convinced of the truth of his beliefs than before."

PEOPLE LATCH ONTO ARGUMENTS THAT SUPPORT WHAT THEY ALREADY BELIEVE AND IGNORE PLAUSIBLE EVIDENCE TO THE CONTRARY.

Think about the conspiracy theories people hold because of what they've been told on social media. Do you think they will learn from their mistakes when it becomes clear they've been misled?

People latch onto arguments that support what they already believe and ignore plausible evidence to the contrary.

Your brain would rather win an argument than get to the bottom of the issue at hand.

If those same aliens were to land on earth today, what they would think about the fact that we have access to the sum of all human knowledge in the palm of our hands and yet a large percentage of the population still believes in conspiracy theories.

Maybe that's why they never showed.

## *Life's tips/3*

"Nothing is so difficult as not deceiving oneself."
*– Ludwig Wittgenstein.*





*Next step*

••• See us about the best investment options for you.

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