



Investment Comments by IMS director: **Selwyn Parker** CFP™, ANZIIF

In my last article I discussed investment markets; personal financial advice; changes expected from the *financial advisers Code Committee*; investing for income in retirement (using fixed interest products). In this issue I comment on the role of equity investments (or shares) as part of your investment retirement strategy.

Market Comments

Following strong share price growth since the low point of mid March 09 the worlds share markets finally stopped for a breather in the 2nd half of January. At the end of January 10 the NZX was up 23% and the MSCI world was up 14% in NZD after giving up -2.0%), and -1% respectively (the ASX -6%) in January. I view the January price correction as healthy for investors and markets alike.

It depends on which commentators you read the bulls or the bears as to which direction the global economy is heading. However my take from various sources is that the world is slowly becoming a safer place to invest again, although the prospects vary widely from region to region. The US (still the largest economy (by a large margin) is clearly on the mend, annualised GDP growth in the December quarter a strong 5.70%. US consumers have increased their spending and consumer confidence is on the rise, exports are going well, and businesses are spending more on equipment. Growth has also been stronger-than-expected in China; the expected power house to global economic growth over the next few years grew by 8.70 percent last year (forecast +9.7% in 2010 and +9% in 2011). The return expectation from shares over the next few years seems relatively attractive to alternative investment options, particularly cash, but this may change if or when interest rates rise or the region's economic outlook changes (*Detailed commentary available on request*).

Investing in Shares for Your Retirement

Shares are partial ownership in a business and its future income stream. Businesses exist only to make more profits than you could normally make elsewhere.

The objective is to find and retain great companies with growing income streams and great profitability. Shares offer higher potential returns than other asset classes but come with higher risk/volatility. They offer 2 forms of return; 1 is cash *dividends* usually paid 6 monthly. The other is the change in capital value from the rise (or fall) in the company's share price.

Dividends are generally consistent each year and taxable, but the capital growth portion is volatile.

For most investors this generally means shares in companies listed on a national stock exchange such as the NZX, but you can also own shares in a privately held company (unlisted).

Share holders rank at the very end of the security queue behind all other creditors. Because share prices and company revenue/profitability are sensitive to changes in the economic cycle or company specific news, so the share price can change without warning. The last thing you want is to be a forced seller when the market is at a very low point, hence invest for 3 to 5+ years to allow you to ride out market down turns. Your reward for accepting this additional risk is an expectation of higher reward over other less risky assets such as (high quality) fixed interest, and cash. The only sure way to minimise investment risk is by diversification. Shares offer diversification from other forms of investment such as property, and fixed interest.

Why Are Shares Important As Part of Your Retirement Strategy?

Most of us are investing for the remainder of our lives so we need to take a medium to long term view when designing and managing your retirement investment portfolio.

Beware; your silent enemy is **inflation**, as a long term investor you need a strategy to protect your savings purchasing power ahead of inflation, e.g. \$100,000 in 10 years time will only purchase \$77,000 of goods if inflation runs at 2.5%pa. That could be 23% of your capital eroded.

Growth assets such as property and shares are generally a great hedge against inflation risk as their capital values generally appreciate ahead of inflation. However, if you have an aversion to shares you can achieve the same objective by retaining the rate of inflation from net interest earned each year. However, you may need more capital to achieve the same (after tax) result.

So if it is that simple why isn't everybody doing it?

NZ has a chequered history of a boom or bust market, remember 87? A general lack of financial knowledge, poor financial advice, and inadequate regulation were all contributors. These issues either have been addressed, or are now being addressed by government.

Before buying any shares first do your research, understand what you are buying, seek qualified advice, and remember share prices will move up and down constantly, and often caused by a myriad of complex issues.

Good advice can be very helpful in volatile markets by disconnecting you from the high emotions and helping you make informed rationale decisions. But also expect to pay for independent advice around say \$150 per hour (you get what you pay for), so shop around.

Always seek your adviser's rationale behind every investment recommendation to buy or sell any financial asset (*disability insurance policies included*); you should not have to ask!

Generally, unless you have financial research skills and heaps of time to research thousands of companies I suggest trading shares on your own is akin to gambling.

Seek out qualified financial advice (or ask your accountant or lawyer for a referral) and consider contracting out those specialist responsibilities. Serious investors should then meet with their financial adviser at regular 6 monthly intervals.

Did you know that there are 166 companies (\$52.5 million) listed on the NZSX, and 2,198 (\$1 trillion) on the ASX, how can you reasonably expect research and monitor them.

What Return Can you Expect from Shares?

When buying or reviewing your shares take a 3 to 5+ year view. Economic conditions will change, share prices will change, this time should allow you to ride out the economic downturn and avoid being a forced seller. In any 1 year period your total return from shares can be negative, but on average investing in a spread of quality shares you should yield a total return (income and growth) close to 8% - 9%pa (pre-tax) on average over a 5 year period. However, timing your entry into the share market can also be very important e.g. buying just before a recession can be costly, so manage this process carefully. International shares offer small dividend payments but more share price growth, also remember when investing outside of NZ that currency risk is very important and needs to be monitored and managed.

How Do I Cash Up My Return?

In retirement your pension can be supplemented from the sale of profits from your shares, however do not rely on capital growth for your regular essential expenditure as when a downturn comes it is often a time to reevaluate and/or hold for better times.

Managed Funds and Investment Trusts and Where Do They Fit in Your Savings Strategy?

A managed fund is where investors pool their money to buy a portfolio of shares, property, or bonds that is monitored and managed by the manager. Managed funds make up an increasing portion of the NZ investment cake with net inflow of \$253 million over the last quarter.

You and yours should already be members of Kiwi Saver, if not talk to me. Outside of Kiwi Saver my preference is to use the cream of the wholesale global *share bargain hunters and stock picker managers*, a strategy that has generally worked well for my clients over the last decade.

For help designing your personal financial strategy or portfolio, talk to a Certified financial adviser, or contact Selwyn Parker (*Certified Financial Planner^{cm}*) directly at IMS **ph 5767286, or 027 658 3263.**

Disclaimer

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