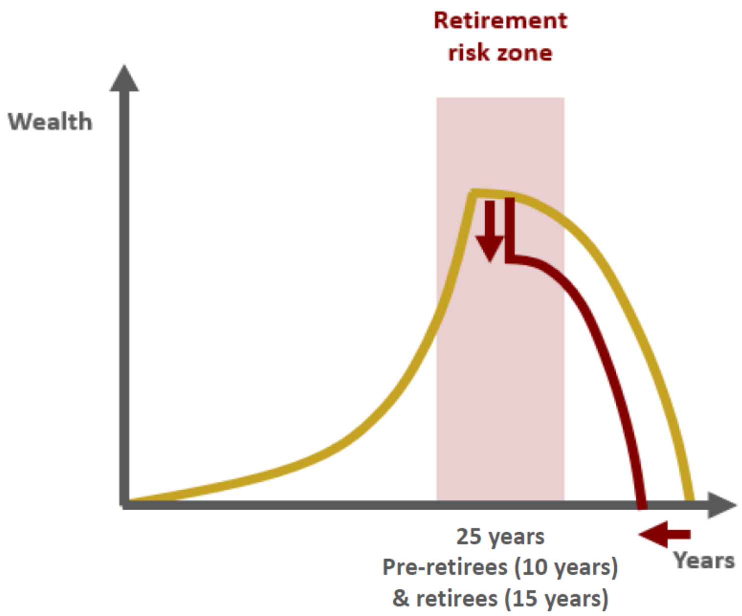
Navigating the Retirement Risk Zone

Jason Teh, Chief Investment Officer at Vertium Asset Management | 21 April 2021

When it comes to planning for retirement, hope is not a strategy. As more Australians transition from wealth accumulation to retirement, there are some key factors to consider as they enter the Retirement Risk Zone.

The Retirement Risk Zone is a critical period in the financial life cycle, spanning about 10 years prior to retirement and 15 years after retirement. It's a crucial time, because when retirement balances are at their peak, they are most vulnerable to a market downturn.

Chart 1: The Retirement Risk Zone



The sequence of returns (sequencing risk) within this period can have a dramatic effect on the longevity of your portfolio. Short-term portfolio losses can have significant long-term effects on retirement savings, compared with similar losses at the early stages of wealth accumulation.

Sequencing risk is amplified as retirement approaches if portfolios are highly weighted to high-risk assets which are more suitable for the accumulation phase. Experiencing a market correction in the Retirement Risk Zone can be very difficult to recover from. If it happens, there are a few options to replace the lost savings – none of which are likely to be acceptable. These include delaying retirement, reducing retirement spend, or simply taking on more investment risk to recover lost returns.

This inherent danger is why portfolio strategies for retirees in the Retirement Risk Zone need to transition towards preserving capital while maintaining a decent income. As you move from accumulating to decumulating wealth, your investment needs and risk profile change. Chasing higher returns decreases in importance and instead receiving income and preserving capital become more important.

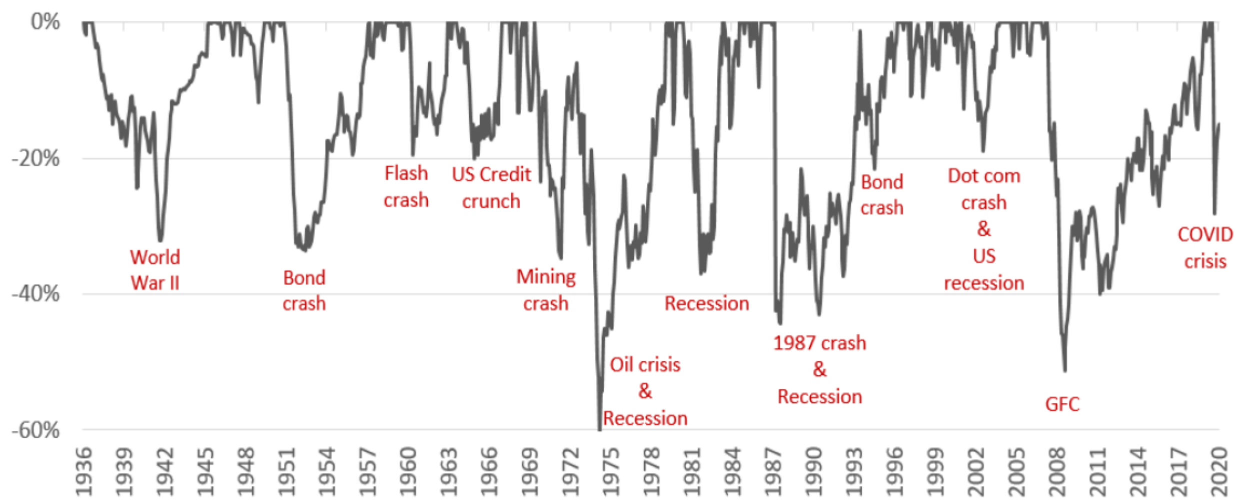
Market corrections will happen

Equities are likely to be part of most retirement plans because they provide long-term returns to hedge against rising living expenses, as well as relatively higher levels of income in an ultra-low interest rate environment. However, equities are the worst asset class when it comes to volatility – especially during market corrections.

It should come as no surprise that stock markets correct whenever global growth slows. This has certainly been the case over the past 30 years, during which time there have been nine global slowdowns.

In fact, in the past 84 years – spanning from World War II to the recent COVID-19 crisis – there have been 12 large corrections, which are defined as drawdowns of 20% or more. That's an average of one big correction every seven years. So it's highly likely that the average retiree will experience a major market correction in the 25 year Retirement Risk Zone.

Chart 2: All Ordinaries Price Index Drawdown Profile



Average of 1 big correction every 7 years

Equity income expertise

One can hope that retirement occurs without a market correction. If you experience strong rising markets within the Retirement Risk Zone, you will more than likely enjoy a comfortable retirement. However, hope is not a retirement plan. Experiencing a market correction during this period could seriously damage your retirement outcome.

Preparing ahead is the best protection within the Retirement Risk Zone by aligning portfolios with the types of assets suitable for retirement. One strategy that has become popular over the past decade is equity income. This strategy has capital preservation characteristics to deliver low downside risk to investors and retirees. Higher income is also a key component of many equity income strategies, with a focus on providing greater yield than cash investments. And unlike cash-based income strategies, equity income has the advantage of providing a hedge against inflation.

Vertium Asset Management, in partnership with Copia Investment Partners, is a specialist Australian equity income investment manager focused on delivering Australians better investment outcomes in the lead-up to and during their retirement.

The **Vertium Equity Income Fund** is suitable for investors looking for lower risk equity market exposure or those drawing down on their savings. The fund invests in quality Australian companies with attractive valuations that pay consistent and sustainable distributions, with the aim of delivering more income with less risk than the Australian share market.

About the author

Jason Teh, Chief Investment Officer
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Jason founded Vertium Asset Management in 2017 and has around 20 years' Australian equity investment management experience. He leads Vertium's investment team and is responsible for the firm's investment philosophy, process and portfolio management.

Before establishing Vertium, Jason was a Senior Portfolio Manager at Investors Mutual. He was the architect of the Investors Mutual Equity Income Fund, which he successfully managed for almost six years. As the second-longest serving employee at Investors Mutual spanning over 16 years, he had a variety of roles including managing a share of the Investors Mutual Australian Share Fund and as an Equity Analyst and Senior Quantitative Analyst.

About Vertium Asset Management

Founded in 2017 by Jason Teh, one of Australia's leading equity income investors, Vertium is a specialist Australian equity income investment manager focused on delivering Australians better investment outcomes in the lead-up to and during retirement.

Vertium is a proud investment manager partner of Copia Investment Partners, an independent multi-boutique investment management group.

Copia provides the resources and infrastructure our team needs to prosper, including distribution, marketing, operations and compliance services, enabling us to focus solely on delivering our investors superior long-term investment outcomes.

Further information

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