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Editorial

The English language is in a continuous state of 'linguistic drift', and some words and phrases we use regularly today will disappear in future, replaced by new expressions. Australians are proud of their local lingo, and each year, the Australian National Dictionary Centre announces a Word of the Year. The words point to events in the headlines each year, such as 'teal' (2022), 'iso' (2020), 'democracy sausage' (2016), 'shirtfront' (2014), 'green-on-blue' (2012), 'vuvuzela' (2010), and 'podcast' (2006).

Even when words stay in common usage, they sometimes develop new meanings, and 'superannuation' is a prime example. Its etymology, or origin, dates to the 1600s, when 'superannuated' meant 'to declare obsolete'. It comes from the Latin 'superannuatus', meaning 'to be too old', from super = over and annus = year. We don't use the word in its old meaning much anymore, but it used to be common to say something was 'superannuated' when it was obsolete due to age or disrepair. We have superannuated our fax machines, our iPods, our VCRs and our old computers and mobile phones.

In fact, the word has gone full circle. Where it meant impaired or disqualified or obsolete due to old age in 1690, it graduated to 'retirement and pension because of age', to today's superannuation which is something we all want more of. It is money to live on in the golden years, for fit and healthy 60-year-olds who expect to live another 30 years. There's nothing outmoded or old-fashioned about superannuation now.

Since 1992, governments have loved the idea of retirement savings so much that they regularly devised clever new ways to allow as much money as possible into super, even with a couple of $1 million opportunities. They came up with cool names like downsizer or salary sacrifice or carry forwards for all these ideas. And the people said: "Gimme more, more, more!"

And then, having set up a system to encourage as much as possible into retirement savings, this glorious thing called superannuation, the authorities suddenly realised it had become an investing nirvana. Low tax, take it out in a lump sum if you want it, leave it to the children, invest in anything. Buy a vintage car, art, wine ... whatever your heart desires.

And then it's ... oh dear ... what have we done? Those wealthy bastards out there are using it for inheritance, not retirement. Some dropkick has $400 million in there. That doesn't sound obsolete.

It's become such a good thing, so simply wonderful and so favourably taxed, that governments are now scrambling to find ways to stop people having too much of it. Or new ways to tax it. It's like: *"Yes, we told you to put as much as possible into super, and we invented new the ways for you to do it. Now, damn well take it out!"*

Last week, Treasury issued a Consultation Paper on the new tax on super balances over $3 million. It's the latest claw-back as governments realise superannuation needs to return to its old roots, strictly to provide for those who are 'too old'.

The paper issued on 31 March 2023 is similar to the original Press Release of 28 February 2023. Treasury still calls it a "*headline tax rate to 30%, up from 15%*", which it is not, because the first 15% is taxed completely differently to the second 15%. And their main justification for the ridiculous decision to tax unrealised capital gains is because it's easy to calculate:

"The approach to estimate earnings seeks to be simple and minimise unnecessary or additional compliance costs by largely relying on data reported through existing arrangements."

There is one clarification on how earnings will be calculated, using the Total Superannuation Balance (TSB):

" ... the previous financial year's TSB will be adjusted to equal $3 million for the purposes of calculating earnings. This approach ensures that any growth in the fund that occurs below the $3 million threshold is not counted as earnings."

Treasury gives this example:

> Tim's earnings are calculated by subtracting the value of his contributions after tax, from his closing TSB, then taking the difference between his opening and closing TSB. As Tim's opening TSB is less than $3 million, for the earnings calculation this will be replaced with a $3 million value. This is to ensure that the earnings calculation only captures the earnings for the part of his TSB over $3 million.
>
> $$\boldsymbol{Earnings} = (\boldsymbol{TSB}_{\boldsymbol{Current\ Financial\ Year}} + \boldsymbol{Withdrawals} - \boldsymbol{Net\ Contributions}) - \boldsymbol{TSB}_{\boldsymbol{Previous\ Financial\ Year}}$$
>
> Earnings = ($3.2 million - $8,500) - $3 million = $191,500

There are 15 consultation questions and the deadline is 17 April for anyone who wants to vent their spleen. In our recent Reader Survey, here are the responses on the $3 million tax from about 800 people. Over 70% in favour, but with most saying the indexation and unrealised capital gains aspects must be addressed.

ANSWER CHOICES	RESPONSES
Yes, super is for retirement spending and $3 million is enough	27.70%
Yes, the Government needs to find new sources of revenue	3.12%
Yes, but the taxing of capital gains and lack of indexing must be fixed first	41.35%
No, people with large balances have used the super system as intended	15.60%
No, if the tax changes, people will find alternative tax-effective structures	12.22%

Yes, superannuation remains a great vehicle to save for retirement, but there is an asset which is even more fundamental for future prosperity. Its benefits transcend the financial and go to the emotional, a place of security, of wellbeing, of lifestyle. It's a place to call home, owning not renting. If there is one thing that beats super hands down in retirement, it is owning a home, a place to rest your head without the fear of a landlord throwing you out. In super, we develop strategies on asset allocation and portfolio construction, but greater focus is needed in financial planning on the route to owning a home.

We duke it out between senior voices in superannuation. **Andrew Gale,** former chair of the **SMSF Association** and leading public policy expert, takes a critical look at the claims that super concessions cost the Budget something like $50 billion a year, arguing the net cost is much lower. And **Brendan Coates and Joey Moloney of Grattan** say we have created a super system where the benefits go to the wealthy and much bigger reforms are needed than the tiny impact of the new $3 million tax.

Then **Andrew Yee of HLB Mann Judd** explains how some of his clients are already reacting to the proposed new tax, especially focussing on assets that can be revalued and generate an unwanted, unrealised capital gain liability.

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On the subject of residential real estate, the market is at a critical juncture with the first month-on-month price rises for a year in March 2023 in **CoreLogic**'s National Home Value Index. Sydney led the way with a 1.4% gain. CoreLogic's Research Director, **Tim Lawless**, said the rise was due to low advertised stock levels, extremely tight rental conditions and additional demand from overseas migration.

"Advertised supply has been below average since September last year ... With rental markets this tight, it's likely we are seeing some spillover from renting into purchasing, although with mortgage rates so high, not

everyone who wants to buy will be able to qualify for a loan. Similarly, with net overseas migration at record levels and rising, there is a chance more permanent or long-term migrants who can afford to, will skip the rental phase and fast track a home purchase simply because they can't find rental accommodation."

CoreLogic Home Value Index, released 3 April 2023

Index results as at 31 March, 2023	Change in dwelling values				
	Month	Quarter	Annual	Total return	Median value
Sydney	1.4%	0.4%	-12.1%	-9.6%	$1,014,393
Melbourne	0.6%	-0.9%	-9.0%	-6.0%	$747,322
Brisbane	0.1%	-1.7%	-8.6%	-4.5%	$698,071
Adelaide	-0.1%	-1.1%	3.0%	6.5%	$645,721
Perth	0.5%	0.1%	1.9%	6.5%	$567,111
Hobart	-0.9%	-4.0%	-12.9%	-9.4%	$650,689
Darwin	-0.4%	-0.9%	1.6%	7.6%	$492,465
Canberra	-0.5%	-2.0%	-8.1%	-4.6%	$828,175
Combined capitals	**0.8%**	**-0.4%**	**-8.7%**	**-5.5%**	**$764,995**
Combined regional	**0.2%**	**-1.0%**	**-5.7%**	**-1.7%**	**$578,486**
National	**0.6%**	**-0.6%**	**-8.0%**	**-4.7%**	**$704,723**

So now everyone is wondering whether March was a one-off before prices continue falling. The fixed rate mortgage cliff is high. My view is not much will happen with prices over the rest of 2023 with forces pushing each way. While we may not have seen the last of the cash rate increases, we are at or near the top, but anecdotal evidence is that inflation is still high. Only 35% of people have a mortgage and the rest will continue spending.

CBA economists pored over the words in the RBA announcement for important subtle changes, and found two:

"In the March Statement accompanying the Board decision it was stated that, *"the Board expects that further tightening of monetary policy **will** be needed to ensure that inflation returns to target"*.

Today that sentence was changed to, *"the Board expects that **some** further tightening of monetary policy **may** well be needed to ensure that inflation returns to target."* (our emphasis in bold).

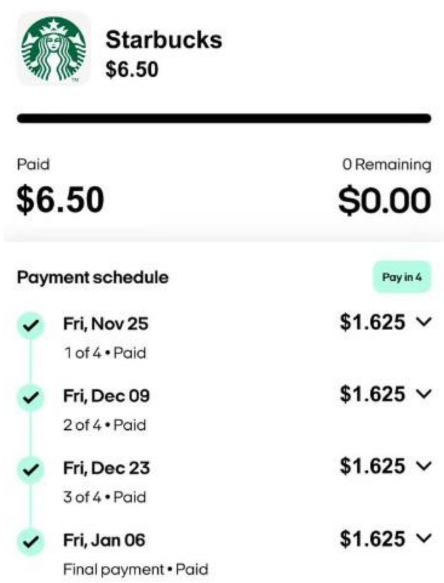
The Governor has inserted the word "some" before the word "further". And more importantly the word "will" has been replaced with "may"."

What games we play! In the hours before the Reserve Bank announcement, economists across the country agonised about their own rate call, feeling the absolute necessity to make one final bid. Is this the best use of the expensive and precious time of so many talented people, to produce contrary pontifications that are confirmed as right or wrong within an hour? Who benefits from that other than a later "*I told you so*" from one and "*They got it wrong*" from another. Here are two from from my mailbox an hour before Phil Lowe's decision:

"We expect the Reserve Bank of Australia (RBA) to pause at the April meeting as it assesses the outlook for the economy and the feed-through of monetary tightening."

"We continue to expect the RBA to increase the cash rate by 25bps at today's meeting, to 3.85%. The labour market and inflation have slowed only modestly meaning additional tightening is still needed."

And if anyone needs evidence that coffee shops can charge almost whatever they wish for an almond milk latte with a dash of pistachio syrup, here's what BNPL financial freedom looks like.



Also in this week's edition ...

Cameron McCormack of VanEck looks at [listed property trusts](#) (A-REITs), many of which have performed poorly in the last 12 months. The crucial question is whether the necessary value markdowns from rising rates and WFH trends are already build into the market prices. **Morningstar's Alex Prineas** believes the downside is mainly priced in as most A-REITs are trading well below their net tangible assets and his valuations, and are stronger than offshore portfolios.

"Australian listed property players have lower gearing, largely locked-in long-term debt, and have limited need to tap debt markets over the next 18 months ... Major REITs in Australia have solid fundamentals."

James Gruber looks at the market narratives and storytelling pitched at investors, but it's the numbers in the company earnings and balance sheets that really matter.

And **Richard Dinham of Fidelity** reports on survey results showing many people enter retirement earlier than they expected, and while anxious at first, they often settle into a more balanced rhythm and acceptance of their circumstances.

This week's White Paper is **VanEck's** latest quarterly economic outlook, encouraging investors to focus on liquidity, strong balance sheets and cash flow, and avoid highly volatile and speculative assets.

Graham Hand

10 reasons owning your home beats super in retirement

Graham Hand

Owning a home - with its tax-free status, exclusion from social security tests and spectacular price rises - has paid off handsomely for nearly every household over the long term. While the superannuation industry implores members to put as much as possible into retirement savings, it is better to buy a home, especially for retirement. Owning a home is as much a lifestyle, security and self-determination decision as it is financial, and most Australians are willing to borrow to the hilt to join the party. The leverage has driven significant wealth creation, and the same people would never dream of borrowing such large amounts to buy shares.

In a speech to the National Press Club on 5 April 2023, Reserve Bank Governor Philip Lowe said:

"The price of land is high because of the choices we made as a society, where to live, how to tax housing and how to invest in transport."

Successive governments have upheld policies making it highly attractive to own our homes, and it's unlikely to change. Over time, Australians have spent an increasing proportion of disposable income on housing, and the willingness to lock into 30-year mortgages sustains prices. Unfortunately, more people than ever cannot afford their own home, and it's made more difficult for them by deposits and income locked in superannuation.

Residential real estate in Australia is overwhelmingly owned by individuals rather than institutions and accounts for most personal wealth. Here are the market sizes:

- Residential real estate, $9.3 trillion
- Australian listed securities, $2.8 trillion
- Superannuation assets, $3.4 trillion
- Commercial real estate, $1.3 trillion

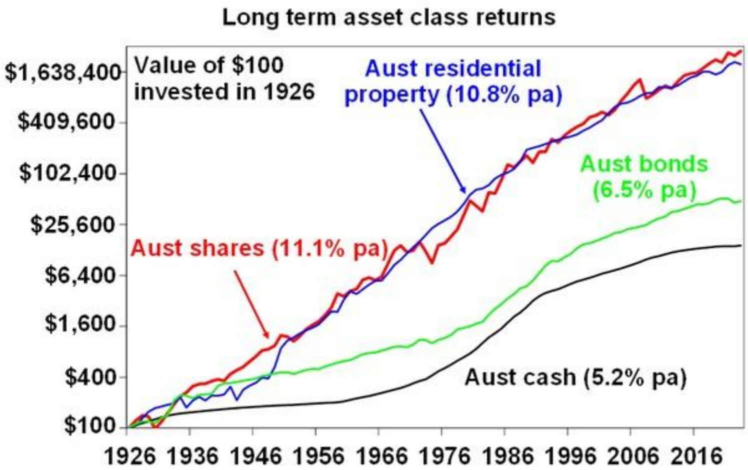
But this article is not about the merits of investing in residential real estate generally. It focusses on owning a home. If anyone with sufficient resources has the choice between owning their home and putting more money into superannuation, the case for the home is strong.

1. Ability to ignore market volatility

"Stocks provide you minute-to-minute valuations for your holdings whereas I have yet to see a quotation for either my farm or the New York real estate ... if a moody fellow with a farm bordering my property yelled out a

price every day to me at which he would either buy my farm or sell me his – and those prices varied widely over short periods of time depending on his mental state – how in the world could I be other than benefited by his erratic behaviour? If his daily shout-out was ridiculously low, and I had some spare cash, I would buy his farm. If the number he yelled was absurdly high, I could either sell to him or just go on farming."
- Warren Buffett.

Given that the long-term returns from residential property are almost the same as returns from investing in local shares, as shown here, why are far more Australians willing to borrow to their maximum potential to buy a home? There are easy ways to gear into shares (geared ETFs, geared managed funds, margin lending, warrants, etc) but the daily mark-to-market of the portfolio is too painful for most to handle. Fortunately, when it comes to a home, despite what Warren Buffett says, nobody stands over the fence of a property and yells out a bid or offer each day. Homeowners hang on and benefit from long-term gains.



Source: AMP

Buyers of their own home have considerable risk tolerance because they think of it as their home first and a long-term investment second, and they are confident that over time, it will increase in value. Losses are not felt as long as mortgage payments can be sustained, and owners do not panic when the headlines scream '*Sharemarket loses $60 billion in a day*' even if residential property prices fall 10% in a year, as they did to March 2023.

From 10am to 4pm every weekday except public holidays, the Australian stockmarket marks a portfolio's scorecard. It tells investors how well or badly they are doing and drives much of the short-term mentality that plagues equity investors. Many equity investors do worse than the index because they buy when markets are high on confidence and sell when markets are low on doom. [Research by DALBAR](#) shows investor behaviour drives returns, with their 30-year data indicating the average investor in the US S&P500 achieved 7.13% while the index delivered 10.65%.

2. Australia's short-term market and rental stress

My wife and I are friends with a couple in their forties who have two primary school children. We met them a few years ago when they lived near us. Their two-bedroom apartment was modest but within their budget, and the school was nearby. Then the landlord told them he was selling the apartment and gave them a month to leave. Stressed and desperate, they eventually found another affordable place but not with good transport, so they moved the kids to a closer school. This apartment leaked and as soon as the 12-month lease was up, they moved again. Overwhelmed by their nomadic existence, they bought a townhouse in the property boom of 2021 after watching prices spiral painfully upwards while they rented.

CPI rents versus advertised rents (2019=100)

Source: RBA.

Contrast this with 1985 when I was working in Switzerland, and a Senior Vice President from Swiss Bank Corporation invited my wife and me to dinner. He proudly showed us around his grand home, including his books filling a library. A big oil tank in the basement to fuel the heating sticks in my mind. I asked him how long the house had been in his family.

"Oh, we don't own it," he said, sounding surprised by my question. "We have a 30-year lease. Why would anyone want to put all their money into a single asset like a house?"

Anybody? Try most Australians. Renters here face the insecurity of short-term leases and the potential to return to the market before they have settled in.

The National Debt Helpline reports that rent is one of the two most-reported worries, and the Reserve Bank has noted that renter stress and affordability are worsening as rents outstrip CPI and renters bid against each other. The cost of renting has become the second-highest component of the CPI.

3. Humiliating renting experiences

Senior superannuation industry professionals argue the merits of super then return each night to a comfortable home where they can knock a nail in the wall without a real estate agent berating them.

Let's put aside the financial aspects and consider what renting in retirement might look like. A 65-year-old is told to leave their home in a month, with the hassle of packing, storing contents, Saturday mornings inspecting new places, moving in, unpacking … and repeating all this a year later.

Here is what the landlord can do, according to NSW Fair Trading.

"A landlord, agent or authorised person acting on their behalf can generally only enter the property without the tenant's consent if they provide notice to the tenant."

Sounds fair, but what are these notice periods?

- To inspect the property: 7 days' notice, up to four inspections a year.
- To assess for maintenance: 2 days' notice.
- To repair a smoke alarm: 1 hour's notice.

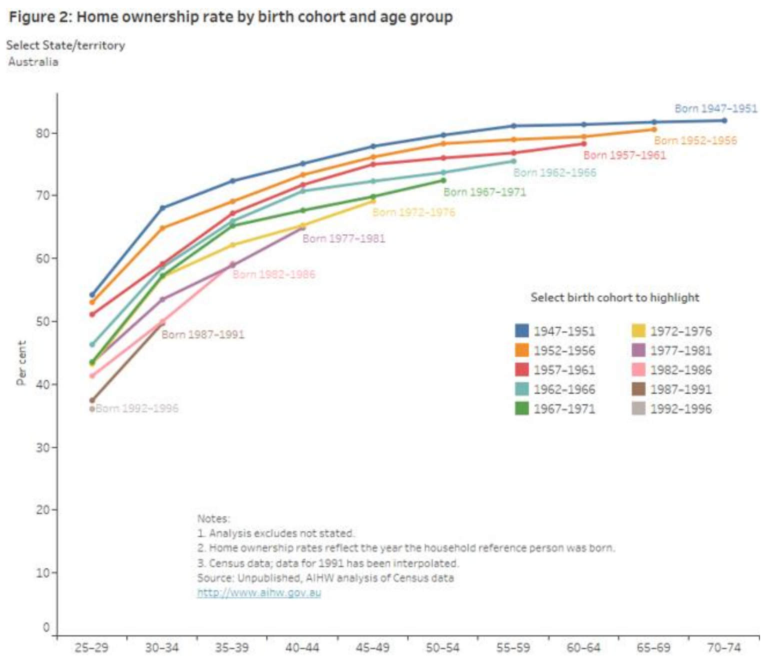
And on it goes. If the property is for sale, the tenant must allow access twice a week on 48 hours' notice and be given reasonable opportunity to move belongings to avoid being videoed or photographed. Check if the bathroom is clean? Please come right in. Imagine someone coming into your home and demanding you move your stuff for a decent photo of your bedroom.

It would take a lot of superannuation to want to go through that experience, then repeat it a year later when the landlord decides to up the rent by 50% or renovate the bathroom. No amount of admiring your superannuation balance compensates for being kicked out of your 'home'.

4. More money needed by subsequent generations

Compulsory superannuation for most Australians was introduced in 1992, starting at 3% of salaries but escalating now to 10.5% on its way to 12%. In previous generations, much of this money would have gone into a home.

In 2021, according to the latest ABS data, of the 9.8 million Australian households, 67% were homeowners, of which 32% did not have a mortgage and 35% did. Home ownership is highest among older people, at around 80%, as younger people struggle to find the required deposits and income.



Click to enlarge

5. Housing shortages and greater competition for renters

Australia is facing a surge in population driven by high immigration levels, and at the same time, housing approvals are down. This table from Westpac shows building approvals, and the vital number, 'Total dwellings', is down 31% from a year earlier.

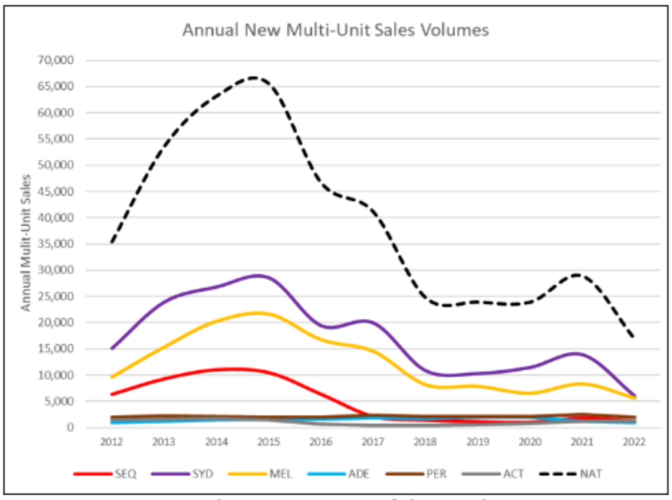
The National Housing Finance and Investment Corporation (NHFIC) estimates Australia will face a shortage of 106,000 dwellings by 2027, with 1.8 million new households forming in the next decade. Fewer apartments are being built, as shown below from Urban Development Institute of Australia (UDIA).

Building approvals – February 2023

		3mth %chg*		%yr	
3mth avg	**latest**	**Jan**	**Feb**	**Jan**	**Feb**
Private houses	8,342	-12.2	-10.2	-12.2	-12.4
Private units	5,187	-14.1	-11.2	-0.5	-16.5
Public dwellings	311	57.7	27.8	55.7	-46.6
Total dwellings	13,839	-12.0	-10.0	-7.0	-15.2
Total dwellings, mthly*	**12,661**	**-27.1**	**4.0**	**-8.1**	**-31.1**
– units in 'high rise'^	3,057	-3.5	-10.7	25.9	-18.2
– units in 'low rise'^	2,430	-9.6	-5.4	-18.6	-18.2
Renovations, $bn	0.996	-5.3	-2.8	-2.6	0.2
Non-res., $bn	4.968	-0.6	-6.6	20.8	8.9

*figures for 'total dwellings mthly' are monthly and mthly%ch, all others are rolling 3mth avg and 3mth%ch; ^all sectors, Westpac estimates
Sources: ABS, Westpac Economics

NATIONAL MULTI-UNIT PERFORMANCE SNAPSHOT, 2022

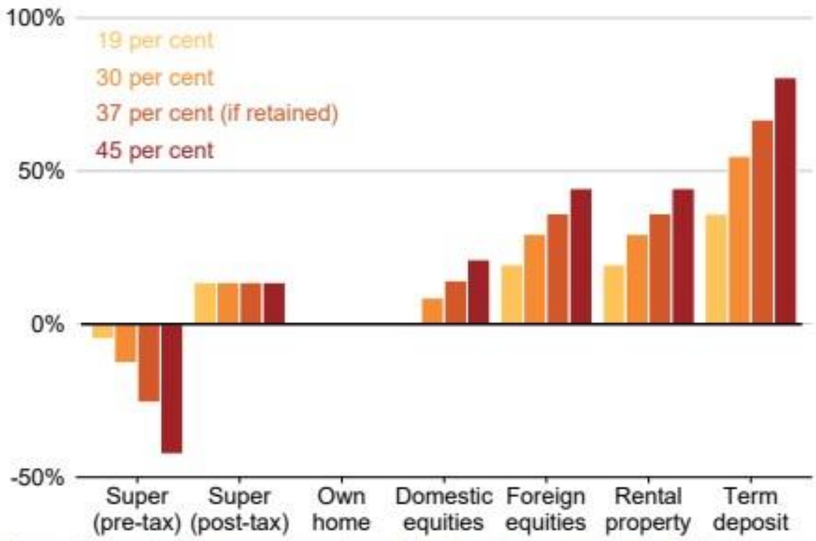


Source: UDIA, Research4 – UDIA State of the Land 2023

Thousands of building companies have collapsed in the last two years, and the most notable recent casualty, Porter Davis, left almost 2,000 homes unfinished.

According to CoreLogic, rents across Australia are 10.1% higher than a year ago, and vacancies are at record lows. Competition for scarce rental properties will only intensify in years to come as 650,000 migrants arrive over two years, with the biggest population rise in Australia's history at about 900,000.

Real effective marginal tax rate on long-term (25 years) savings vehicles by marginal income tax rate



Notes: Grattan Institute recommends retaining the 37 per cent bracket for incomes between $120,000 and $200,000. Real effective marginal tax rates calculated against a expenditure tax benchmark.

Source: Grattan analysis. See Appendix A for details.

6. Better tax breaks for homes than non-concessional super

While superannuation is lauded for its tax advantages, the only savings vehicle with a lower marginal tax rate than an own home is pre-tax (concessional) super, which is limited to $27,500 a year. For people on lower incomes, the tax in super of 15% may be higher than their marginal tax rate.

This chart from the Grattan Institute shows the tax advantages of owning a home.

7. Home ownership assumed in retirement standards

The most-commonly referenced amounts required to live a comfortable or modest lifestyle in retirement are the ASFA Standards.

Comfortable lifestyle (p. a.)		Modest lifestyle (p. a.)	
Couple	**Single**	**Couple**	**Single**
$69,691	$49,462	$45,106	$31,323

What is often overlooked is the short explanation in the footnotes to the tables, which is not even mentioned in the document showing the detailed break up:

"Both budgets assume that the retirees own their own home outright and are relatively healthy."

So even the Association of Superannuation Funds of Australia (ASFA), the body representing large super funds and industry service providers, assumes home ownership before advising members how much money they need to meet a given lifestyle.

8. Social security incentives

The Principal Place of Residence (PPR) is excluded from capital gains tax on personal income and from asset eligibility tests for age pension and other social security pensions. However, superannuation assets are included, which means a person with a large super balance may not qualify for social security and the related health and pensioner benefits, but another person with the same value of assets held in a PPR qualifies. The full age pension for a couple with supplements is $1,604 a fortnight or $41,704 a year. That's an annual incentive to buy a house rather than put more into super.

There is a concession to home ownership in the assets test. For example, a homeowner couple is eligible for a maximum age pension when assets are $419,000 or less (excluding the value of the home) whereas a non-homeowner couple is allowed a higher level of $643,500.

The Government even issues a sort of warning not to sell the family home. How much more privileged can an asset be?

"Your family home, if you live in it, isn't counted as an asset. However, if you decide to sell, it could affect your pension."

9. An alternative source of money to live on

The Home Equity Access Scheme (HEAS, formerly the Pension Loan Scheme) allows homeowners to use real estate as security to generate retirement income. There are also many commercial home equity access schemes which offer different characteristics.

We have discussed the HEAS previously and the full terms are described here. A few key features are:

- The pension payment can be up to 150% of the maximum pension rate. That is $60,000 a year for a couple.
- It is available to people who are not on a government pension.
- There is a no negative equity guarantee, meaning the amount owed on the loan can never be greater than the market value of the property less any mortgage.
- Lump sum advances are possible.

Loan payments are only required from the estate or when the property is sold, and the current interest rate is an attractive 3.95%, although this may increase.

10. The value of 'psychic income'

In a world where it's easy to know the price of everything and the value of nothing, living in your own home carries considerable non-financial rewards. Economists call it 'psychic income' when pleasant surroundings, safety, security and even prestige contribute to wellbeing in a way not measured in money terms.

Once on the property ladder, especially in a house with land, there is often potential to invest in the value of the asset for personal use and financial gain. Fix the bathroom, install a new kitchen, build a sunroom and extra bedroom on the back - these are all great ways to invest in an asset over time, improving surroundings and lifestyle as financial resources and time allow. Many Australians have renovated their way to financial freedom after a modest start.

And here come some caveats ...

W could double the length of this article with qualifying statements, as every person is different.

Yes, some landlords reward good tenants, maintain their properties and rollover leases year to year.

Yes, new homeowners who bought at the peak in 2022 now face rising interest rates and mortgage stress. This article is not arguing everybody should own a home, as borrowers need the financial resources to service their debt.

Yes, the case for the most tax-advantaged, concessional amounts up to $27,500 a year into super is stronger than the non-concessional contributions from after-tax resources.

But, but ...

Arguments about the right time to buy could be made at many times in the last 100 years. The home I bought in 1989 was worth less four years later in 1993 (after 'the recession we had to have') but we did not sell until 2020. Baby Boomers did not pay 11 times earnings for properties but interest rates were far higher.

Renting in Australia is not a pleasant experience for many people. It is made more frustrating by successive government policies that have encouraged home ownership to such an extent that younger generations are locked out of the opportunity that their parents and grandparents took for granted.

As Governor Lowe said, that's the unfortunate reality of the system we have created. It would be political suicide, for example, to tax capital gains on a family home or include the PPR in the assets test for the age pension. No government will go there. The advantages of home ownership are unlikely to disappear, and it's more important for financial plans to consider the journey to home ownership than how superannuation should be invested.

Graham Hand is Editor-At-Large at Firstlinks. This article is general information and does not consider the circumstances of any investor.

The net cost of super concessions is not so gross

Andrew Gale

A more-informed debate on the cost of superannuation concessions is needed. The number dominating the headlines recently is that the concessions are costing $52.5 billion a year but this estimate has not been robustly challenged. By highlighting the gross cost rather than allowing for offsets, it significantly overstates the cost of concessions and has the potential to mislead the debate.

As mentioned in my article last week, the 2021 Intergenerational Report (IGR), forecast changes in government expenditure to be as follows:

Government Expenditure	% of GDP (2021-22)	% of GDP (2060-61)
Health	4.6%	6.2%
Aged Care	1.2%	2.1%
Age and Service Pension	2.5%	2.1%

Superannuation, strongly encouraged by appropriate concessional treatment, is playing a valuable macro role, and the *real* aggregate cost of superannuation concessions, should be interpreted in this light. As superannuation continues to mature, the reduction in age pension costs (as a % of GDP) is a welcome development. Notwithstanding this macro view, the need to address equity and fairness issues in super remains.

Where do the tax concessions arise?

The loudly-trumpeted $52.5 billion is sourced primarily from Treasury's tax estimate figures in the Tax Expenditures and Insights Statements (TEIS) for 2022-2023. Treasury uses this definition:

"A tax expenditure arises where the tax treatment of a class of taxpayer or an activity differs from the standard tax treatment (tax benchmark) that would otherwise apply. Tax expenditures can include tax exemptions, some deductions, rebates and offsets, concessional or higher tax rates applying to a specific class of taxpayers, and deferrals of tax liability."

The TEIS shows the three major items contributing to revenue foregone are:

- Capital Gains Tax (CGT) main residence exemption - $48 billion
- Rental deductions - $24.4 billion
- CGT discount for individuals and trusts - $23.7 billion

The major components of the so-called superannuation concessional tax costs (2022-23 estimates) are:

- Employer superannuation contributions - $23.3 billion
- Superannuation entity earnings - $21.5 billion
- Deductibility of insurance premiums inside superannuation - $2.38 billion
- Personal superannuation contributions - $1.55 billion
- Non-superannuation termination benefits - $1.55 billion
- CGT for superannuation funds - $1.35 billion

Lots of targets there for opponents of superannuation concessions.

Treasury recognises the weaknesses

The problem is that the Treasury tax estimates are an unreliable guide to the real cost of concessions, or the revenue gain if government removed or reduced the concession. For example, they don't allow for social security offsets or behavioural responses if concessions were removed.

This is explicitly acknowledged by Treasury in the most recent Tax Benchmark and Variations Statement:

"*Revenue forgone estimates reflect the existing utilisation of a benchmark variation and do not incorporate any behavioural response which might result from a reduction or removal of the variation to the tax benchmark. They measure the difference in revenue between the existing and benchmark tax treatments, assuming taxpayer behaviour is the same … revenue forgone estimates are* ***not estimates of the revenue increase if a variation to the tax benchmark were to be removed****.*" (my bolding)

A similar statement appears in the TEIS.

These caveats are overlooked in the general commentary on the cost of superannuation concessions, including by Government, the Australia Institute, the Grattan Institute and most of the media who rely upon these information sources. These figures, or at least the use of these figures, are used for a purpose for which they were not intended.

Insufficient analysis has been done on the real cost, or net cost, of superannuation concessions.

A robust attempt was made by the Association of Superannuation Funds of Australia (ASFA) in 2016 ('Mythbusting Superannuation Concessions – March 2016') which concluded that the real cost of concessions was just over half the gross cost, as follows (note at the time that the estimated cost of concessions was $30 billion):

- Annual reduction in age pension expenditure as a result of super: $7 billion
- Impact of behavioural change (people shifting money from one tax-effective vehicle to another) that would occur if super tax concessions were removed: $7 billion
- Real cost: $16 billion

The SMSF Association (SMSFA) reached similar conclusions in its submissions to the Tax White Paper (2015) and the Tax Expenditure (TES) Consultation Paper (2017). The SMSFA concluded an even lower net cost using slightly different methodologies, noting that that:

"the TES measurements of superannuation tax concessions … have the following unrealistic assumptions:

1. *They are measured against a 'comprehensive income' benchmark which measures tax concessions against an idealised tax system where all income is taxed at people's marginal tax rates. The choice of this benchmark has a substantial influence of the cost of the concessions.*

2. *The measurement ignores the fact that people may seek other concessions such as discounted capital gain investments or negatively-geared investments to minimise their tax liability."*

To arrive at a net cost of superannuation concessions needs allow for offsetting social security costs as a result of building healthy superannuation balances.

Retirement Income Review (RIR)

Even the esteemed RIR relies almost entirely on gross costs in its commentary and quantification of the costs of superannuation concessions, largely consigning estimates of net costs (to allow for behavioural changes) to the 'too hard' basket.

It observes that people with very large superannuation balances can receive large superannuation earnings tax concessions, including that:

- In 2018-19, a person with a superannuation balance of $5 million would have received, assuming a net earnings rate of 6%, around $70,000 in earnings tax concessions
- Using the same assumptions, a person with a superannuation balance of $10 million would have received more than $165,000 in earnings tax concessions.

(In a footnote, it states that this assumes all superannuation assets are held in the accumulation phase, the assets would be taxed at the person's marginal tax rate including the Medicare Levy if they were not held in superannuation and there are no unrealised capital gains).

But the RIR also notes:

"This Review uses a comprehensive income tax benchmark to measure the cost of superannuation tax concessions. This means tax revenue actually collected is compared with the estimated amount that would have been collected if contributions and earnings were all taxed at full marginal rates."

So the RIR makes (or relies on) the same assumptions as Treasury.

Whilst not advocating for a continuation of the current level of concessionality for very large account balances, the narrative needs to be better informed.

It is worth noting that the RIR does quote some Treasury work on page 418 which attempts to account for a reallocation of savings if the concessions ('revenue forgone' or RF) did not exist. These 'revenue gains' (RG) are estimated for employer contributions and the earnings tax concession. However, the RIR largely dismisses them because:

"... the RG earnings estimate is 14% lower than that for RF. This is because the earnings on these alternative tax-preferred vehicles are subject to lower marginal tax rates than those used in the RF estimate."

However, it is not clear what assumptions Treasury makes regarding alternative investments outside superannuation, including shares with franking credits, negatively geared property investment and the likely increased utilisation of family trusts and company structures.

Further, the proposed Stage 3 tax cuts will widen further the gap between the gross cost of concessions and the real or net costs.

Will the cost of superannuation concessions exceed age pension costs?

As an added perspective to colour the debate, commentary regarding super concessions is often claimed to ultimately 'cost' more than the age pension. On 20 February 2023, Treasurer Jim Chalmers said:

"Right now, we're on track to spend more on super tax concessions than the age pension by around 2050. I'm not convinced that's a sustainable way to get to our destination – good retirement incomes for more Australians, now and into the future."

The framing of these comments infers a material problem rather than a natural, intended and overall positive outcome of public policy design. That said, I acknowledged in my previous Firstlinks article the need to reduce concessions on very high account balances.

One source for the Treasurer's comments is potentially the RIR which observed that:

"Government expenditure on the age pension as a proportion of GDP is projected to fall slightly over the next 40 years to around 2.3%. Higher superannuation balances reduce age pension costs. The cost of superannuation tax concessions is projected to grow as a proportion of GDP and exceed that of age pension expenditure by around 2050. This is due to earnings tax concessions. The increase in the SG rate to 12% will increase the fiscal cost of the system over the long term."

Again, all these observations are based on the gross cost of superannuation concessions. Different conclusions would apply if the real cost of superannuation concessions were used.

With an ageing population, which will drive increasing aged care and health costs (as a % of GDP), the fact that the cost of age pension will be declining (as a % of GDP) is a notable and positive achievement.

Address high balances but inform the debate properly

Treasury admits its estimates of the cost of superannuation concessions represent gross costs, and a closer examination suggests the real cost may arguably be closer to 60% of the popularly-quoted level.

Whatever the figures, superannuation concessions need to be sustainable and to have a higher degree of equity and fairness, but they meet neither criterion at the moment.

Whilst not advocating for a continuation of the current level of concessionality for very large account balances, the narrative needs to be better informed. The net cost to the public coffers should allow for behavioural change and social security offsets.

Andrew Gale is an actuary, public policy expert in financial services, a non-executive director and a former Chairman of the SMSF Association. The views expressed in this article are focussed on public policy and are personal views not made on behalf of any organisation. This article is not financial or tax advice and it does not consider the individual financial circumstances of any person.

Cut tax breaks to make super fairer and budget stronger

Brendan Coates, Joey Maloney

Australia's $3.3 trillion superannuation system is supposed to boost people's retirement incomes. The Government says as much in its proposed legislated objective for superannuation. The system is supported by billions of dollars of tax breaks each year, ostensibly to that end.

But there's just one problem. Increasingly, much of what is saved is never spent.

Our new report, Super savings: Practical policies for fairer superannuation and a stronger budget, points out that without an overhaul, super tax breaks are set to do little more than boost the inheritances of Australians with well-off parents.

Super contributions and super earnings are both taxed more lightly than other income. These tax breaks cost the Budget about $45 billion (2% of Australia's gross domestic product, or GDP) each year. Here's a reminder of the major tax concessions afforded to super.

Superannuation benefits from significant tax breaks

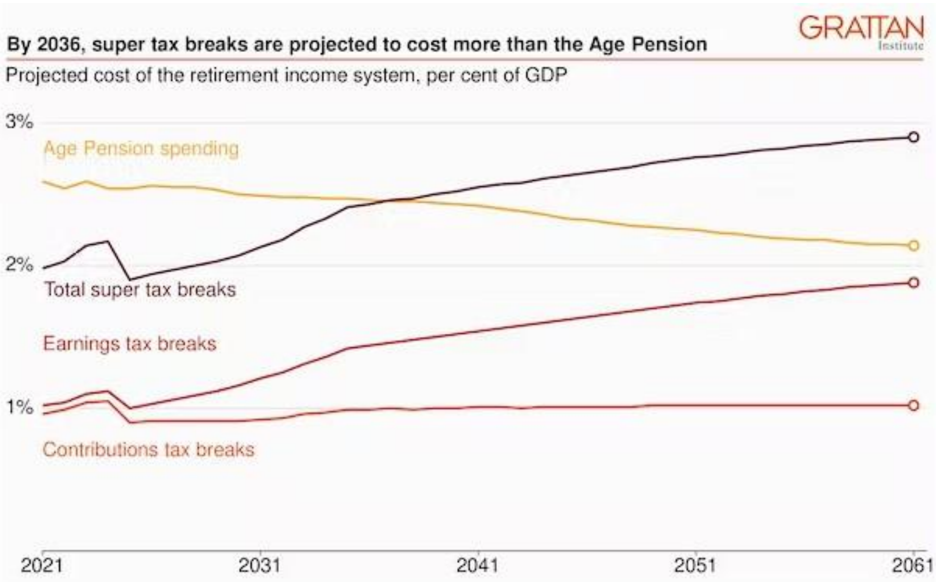
	Accumulation	Retirement
Contributions	• Employers must contribute 10.5 per cent of employees' earnings (rising to 12 per cent by 2025); individuals can make extra voluntary contributions • Contributions are taxed at 15 per cent up to $27,500 a year, and 30 per cent for people earning more than $250,000 • The Low-Income Superannuation Tax Offset (LISTO) refunds contributions tax paid, up to $500, for people earning less than $37,000 • Further post-tax contributions can be made up to a cap of $110,000 p.a. if younger than 75 and with a balance less than $1.7 million (rising to $1.9 million by mid-2023)	• All contributions allowed until age 74 (pre-tax contributions subject to employment requirements) • Only mandated employer contributions and 'downsizer' contributions allowed if aged 75+
Earnings	• Super contributions are invested, earning returns • Those earnings are taxed at 15 per cent in the fund (10 per cent for capital gains)	• Earnings in retirement are untaxed up to a maximum balance of $1.7 million (rising to $1.9 million by mid-2023)

Withdrawals	• No withdrawals until preservation age (60 for future retirees) • Early release for financial hardship is taxed between 17 per cent and 22 per cent if younger than 60	• Payouts are untaxed past preservation age • Bequests taxed depending on the beneficiary, and the share of contributions that were pre-tax

Note: People with balances of less than $500,000 can access 'unused' pre-tax contributions cap space from up to five years prior to make additional pre-tax super contributions.

Source: ATO.

Treasury predicts that the cost to the Budget will hit 3% of GDP by 2060, and that the cost of super tax breaks will overtake the cost of the age pension by as soon as 2036.



Superannuation benefits favour the wealthy

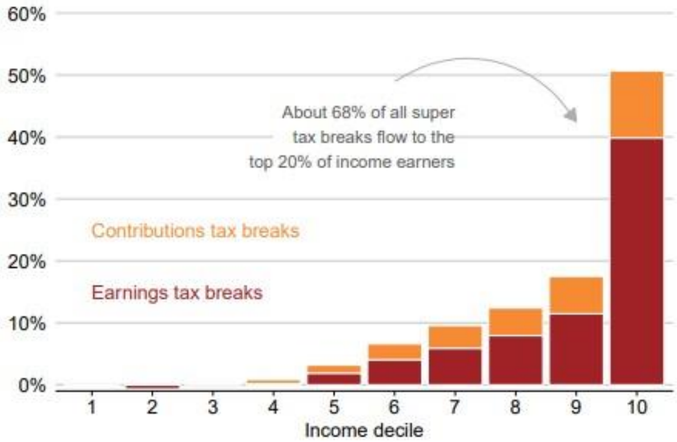
These tax breaks are not well targeted. Two-thirds of their value benefit the top 20% of income earners, who are already saving enough for their retirement. Retirees with big superannuation accounts pay much less tax per dollar of super earnings than younger workers do on their wages.

Much of the boost to super balances from tax breaks is never spent. By 2060, one-third of all withdrawals from super will be via bequests – up from one-fifth today.

Super has become a taxpayer-funded inheritance scheme. Reining in super tax breaks is a responsible way to boost government revenues in a world where the government has committed to higher spending on defence, healthcare, aged care, and disability care.

Governments have supercharged demographic pressures by introducing generous tax concessions for older people. A 'self-funded' retiree couple can have, from 1 July 2023, $3.8 million in super, unlimited home equity, and income outside super up to about $66,000 a year, and pay no income tax. The share of households older than 65 paying tax has halved over the past two decades, and average income tax paid has barely changed for people older than 65, despite strong growth in their incomes and wealth.

Share of total super tax breaks by type and income decile



A reform package to address the inequities

We recommend a reform package that would save the budget more than $11.5 billion a year, including:

- Raising Division 293 tax, which curbs tax breaks to high-income earners on their pre-tax super contributions, from 30% to 35%, and lowering the income threshold at which the tax applies, from $250,000 to $220,000 a year. This would save the budget about $1.1 billion a year and stop many high-income earners benefitting from larger tax breaks, per dollar contributed to their super, than low- and middle-income earners.
- Lowering the cap on pre-tax super contributions, from $27,500 to $20,000 a year. This would save about $1.6 billion a year, mostly by reducing voluntary contributions made by older, wealthier Australians to minimise their income tax bills.
- Abolishing carry-forward provisions and government co-contributions, which were intended to encourage catch-up contributions but in fact facilitate tax minimisation. This would save about $1.1 billion a year.
- Taxing all superannuation earnings in retirement at 15% – the same rate that applies to super earnings before retirement. This would save more than $5.3 billion a year.
- Taxing earnings on super accounts larger than $2 million – rather than $3 million as proposed by the Albanese Government – at 30%. This would save about $3 billion a year, compared to about $2 billion a year under the government's plan.

The warning signs are everywhere. Australia's current superannuation system is unfair and unsustainable. The reforms we recommend would make the system fairer and the budget stronger.

For more details and background information, see the Full Report.

Joey Moloney is Senior Associate and Brendan Coates is the Economic Policy Program Director and a Fellow at Grattan Institute. This article is general information and not personal advice.

What's worrying SMSF trustees about the super tax proposal?

Andrew Yee

The Federal Government is seeking to increase the tax on super balances over $3 million. Here are some of the possible issues with the super tax, as well some observations based on client discussions with SMSF trustees.

Brief recap of the proposal

- If passed, the changes will apply for the 2026 financial year, commencing 1 July 2025. The details still need to be developed and legislation drafted.
- The changes will apply to individuals (not superannuation funds) with a Total Super Balance (from all their super funds) in excess of $3 million on 30 June 2026.
- A new tax of 15% will be levied on the 'earnings' derived from their TSB above $3 million. This will be in addition to current superannuation income tax rate of 15%, applying to the whole of fund earnings.
- Unrealised capital gains ('earnings') will be taxed in a radical change in a tax system that currently only applies tax on income received and realised gains from the sale of asset.
- Unrealised losses can be carried forward, but will not result in a tax refund.
- The individual can elect for their superannuation fund pay the tax. The tax collection mechanism will be similar to the collection of Division 293 tax on concessional superannuation contributions for high income earners.

Possible issues and ramifications of the new tax

Anyone impacted by the changes will need to assess the benefit of holding more than $3 million in superannuation and whether it would be more tax effective to invest the excess in other tax entities, especially other vehicles that don't tax earnings on an accruals basis.

There remains a question, however, whether members who are not yet retired, or who have not met a condition of release to access their superannuation benefits, will be able to move their excess balance out of super.

The $3 million threshold and tax applicable is tested only at year end which may be unfair when fund asset values fluctuate throughout the year.

The new tax is levied on individual superannuation balances and not couples or families. A couple can avoid the tax if the total of their combined TSB is under $6 million and neither of them individually exceeds $3 million. Whereas where one partner has say $5 million in super and their partner has zero superannuation, then the new tax would apply.

It will encourage family tax planning strategies by building up the superannuation balance of family members who are below the $3 million threshold and reducing balances of family members above the $3 million threshold, perhaps via recontribution strategies or contribution splitting.

Asset allocation in superannuation funds may also be affected. It may discourage investment in high growth (but low or no income yielding) investments and illiquid assets such as real property.. Some members may not hold enough cash to the pay the tax, which means the tax may be paid by the member personally.

Elderly people may consider taking out all their superannuation above $3 million to avoid the extra tax, as well as addressing the possibility of the superannuation death benefits tax of up to 17% earlier than otherwise.

Observations from SMSF clients

Clients are generally accepting of tax reform on superannuation provided it is fair and not retrospective and they are not forced to take out superannuation that is already in the system. The proposed changes seem to achieve that.

However many clients have complained about the way the new tax is calculated, in particular basing the tax on a $3 million cap at year end and the calculation of taxable income based on unrealised earnings.

We are already seeing clients reconsider whether to hold illiquid assets, such as property, in their SMSF, especially where the investment would rely heavily on capital gains rather than income for its returns.

Many clients opt for an SMSF to invest in unlisted, private or closely-held investments such as private equity or business real property. They usually cannot invest their superannuation in these type of assets through other superannuation vehicles such as public funds.

These SMSF clients are thinking these assets may be better sitting in another type of entity. Property and private equity may be removed from super where there are no liquidity events.

Overall, clients are talking about a re-allocation of capital to more income-producing, or high-yielding and possibly higher risk assets in superannuation in order to have the liquidity to pay the new tax.

Where to from here?

The client process on the proposed new tax has to date focused on education as opposed to immediate responsive action.

We are telling clients not to panic because we have not seen the full details yet. There may be changes after the consultation process. Clients may commence minor planning but we're telling them not to over plan as commencement is two years from now.

But it is clear that the new tax will encourage those with more than $3 million in superannuation to look at ways to reduce their superannuation benefits. It will also discourage those with less than $3 million to grow their superannuation balance to more than the new tax threshold.

Andrew Yee is Director of Wealth Management at [HLB Mann Judd, Sydney](). This article is general information and does not consider the circumstances of any individual.

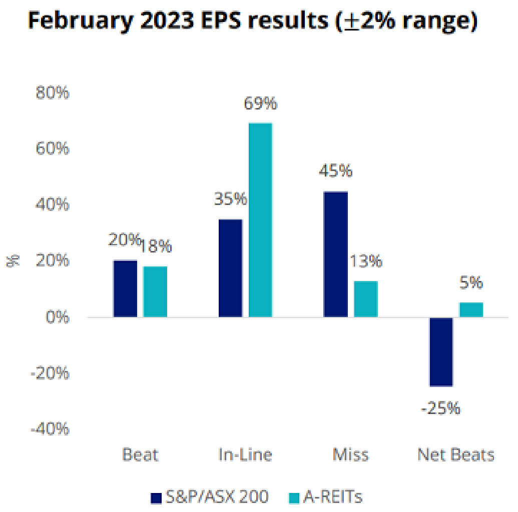
What are the industrial, office or retail listed property picks?

Cameron McCormack

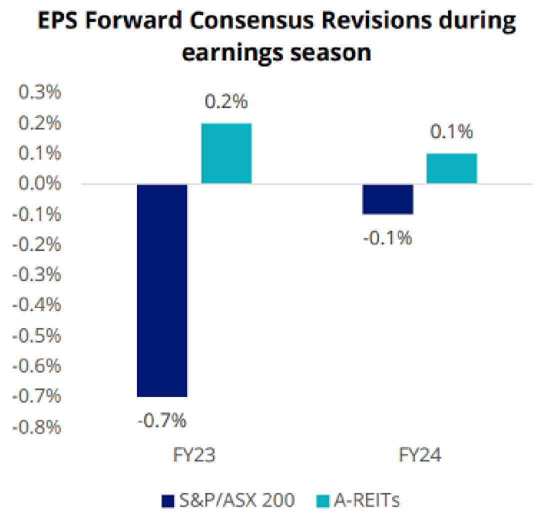
Australian listed property trusts, often called A-REITs, are well positioned for an environment of elevated inflation and low growth. Commercial leases in office, industrial and logistics typically have inflation-linked annual increases in rents written into multi-year contracts, providing inflation protection on income. A-REITs have deleveraged since the GFC and offer exposure to subsectors with inelastic demand for their services in an environment where the global economic activity is subdued.

In the recent Reporting Season, A-REIT earnings results were ahead of the S&P/ASX 200 with earnings per share (EPS) beats higher than misses by 5%. On forward consensus, A-REIT FY23 and FY24 Earnings Per Share (EPS) revisions were upgraded whereas S&P/ASX 200 revisions were downgraded.

Despite rising rates, A-REITs reported a smaller than expected expansion in cap rates (required yield on a property) and drop in net tangible assets ending December 2023. Disappointing results from resource mega caps BHP and Rio Tinto dragged on the equity benchmark index.



Source: Bloomberg, Index Weighted. A-REITs is S&P/ASX 200 A-REITs Index.



Source: Refinitiv. Index weighted. A-REITs is S&P/ASX 200 A-REITs Index.

As we near the second half of 2023, we favour industrial and retail REITs in Australia and globally as both subsectors have shown improvements in occupancy rates. We prefer exposure to Australian REITs as the economy is better positioned than most countries to manage economic challenges in 2023 and fundamentals are also more attractive at an asset class and subsector level.

Three sector potential with stock examples

Let's consider three sectors - industrial, office and retail - with stock examples in each.

1. Industrial REITs

We are overweight Australian industrial REITs. Occupancy rates are lower and market is more concentrated with Goodman Group holding majority market share, restricting barriers of entry.

Industrial REIT cap rates and net operating income in Australia and globally are likely to remain sticky as tenants look to manage excess inventory levels and expand e-commerce channels amid low vacancy rates. Retailers will continue to invest in optimising delivery chains as they address demand for both in-store and online consumer spending. E-commerce and industrial demand are firmly anchored in the economy and remain resilient in the face of slower growth.

Goodman Group (ASX:GMG)

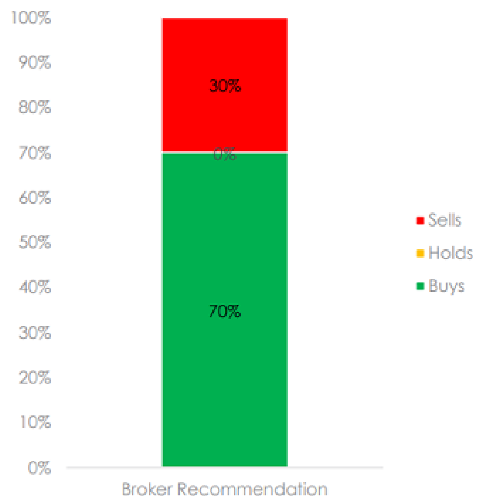
Goodman Group was one of the worst performing REITs over the past 12 months following the recalibration in valuations as markets priced in higher interest rates. Strong sales and earnings growth resulted in Goodman Group becoming one of the most expensive ASX-listed REITs which quickly unraveled during the 2022 asset deflation bear market.

During the February 2023 earnings season, Goodman Group HY23 EPS came in line with expectations and forward guidance was upgraded to 13.5% (from 11%). VanEck see this as achievable given Goodman has major market share across industrials with rental growth expected to remain elevated, local vacancy rates and new market pipeline low.

Median Broker Consensus Share Price 12-month target (+12%)

Source: Bloomberg, As at 28 February 2023.

Broker buy/hold/sell split (10 analysts)



Source: Bloomberg, As at 28 February 2023

2. Office REITs

Office REITs were the worst performing subsector in Australia and globally over 12 months. The rising interest rate environment and adoption of hybrid working environment contributed to less demand for office space, a double headwind for performance.

Despite office REITs trading at a discount to NTA and ratio lower than the benchmark, we favour an underweight position given the secular headwinds emerging particularly globally. The US economy is likely to contract at the end of the year with the unemployment rate expected to rise, reducing demand for office space. This environment will give businesses more buying power when negotiating office leases. Office REITs will also need to expand capex to further attract tenants, putting downward pressure on margins. Senior executives mandating employees back to the office will be muted given the economic slowdown anticipated.

Quality office REITs with sought after space in good locations and amenities will remain attractive. We expect that top-tier office towers to provide uplift in rental growth, while older office buildings will likely be less favourable.

We prefer Australian office REITs exposure relative to global. The US great resignation that played out following COVID-19 saw employees move outside of the bigger cities negating the need for office space. A return to office in the major US cities would require a multi-year transition, keeping occupancy rates low. The great resignation in Australia was smaller hence why we see occupancy rates remaining elevated relative to the US. The Australian economy is also better placed considering the anticipated influx of skilled migrants in 2023 creating further demand for office space.

Dexus (ASX:DXS)

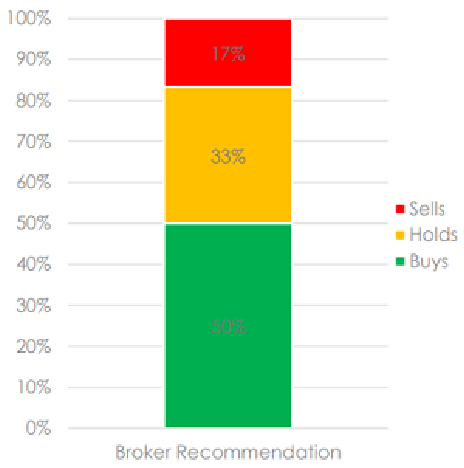
Office REIT Dexus was one of the worst performing stocks over the past 12 months in the A-REITs sector, following the valuation re-rating in a high interest rate environment. During the February 2023 earnings season, Dexus reported high occupancy levels above 95% and relatively prudent balance sheet with 25.6% interest rate hedging, reinforcing the resilience of the portfolio compared to the broader market.

Dexus collects approximately 70% of its income from office rent, of which 50-55% is from Sydney CBD. Given the economic uncertainties surrounding the Australian economic and implications on office REITs leads to our cautious view on the company's outlook in 2023.

Median Broker Consensus Share Price 12 month target (+13%)

Source: Bloomberg, as at 28 February 2023.

Broker buy/hold/sell split (12 analysts)

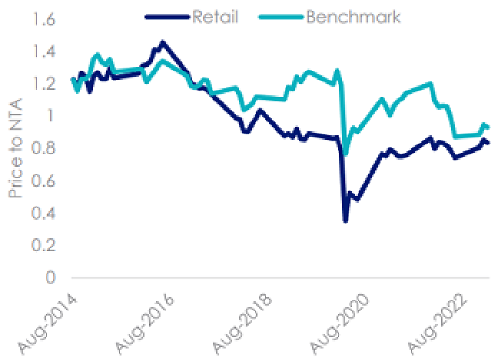


Source: Bloomberg as at 28 February 2023

3. Retail REITs

Retail REITs led the asset class over 12 months in Australia and globally. This strong performance was primarily driven by a reversion to pre-COVID retail conditions from increased customer foot traffic, surge in retail spending and occupancy rates. Retail sales growth ahead of pre-covid trends, multi-decade low unemployment and high wage growth globally highlights broad labour market resilience and scope for customers to maintain healthy discretionary spending.

Australia Price to NTA



Source: Bloomberg, Office as Dexus. Benchmark as MVIS Australia A-REIT Index.

Australia Occupancy Rates

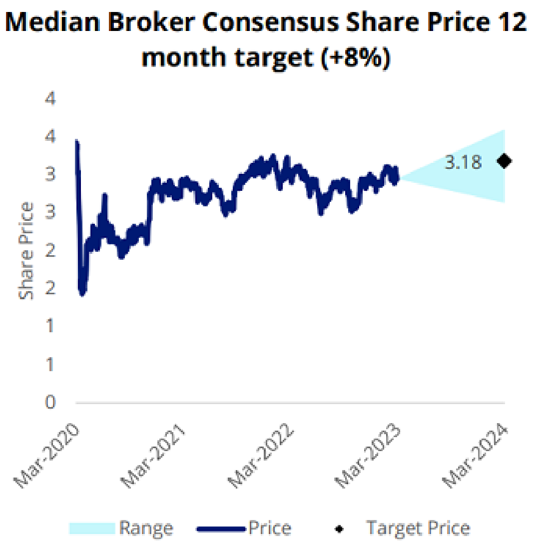
Source: Bloomberg, Macquarie Research, As at 31 December 2022. REIT as equal weighted average of industrials, retail and office. Retail as equal weighting of VCX, GPT, SCG, SGP, MGR, CQR, SCP, HDN.

Looking forward, we are optimistic on the subsector's near term outlook but favour exposure to global REITs relative to Australia. The subsector is well-equipped to benefit through inflation-protected rents despite softer anticipated customer spending following rate hiking cycles. However, Australian consumers will see a more immediate impact from rate rates. Price to NTA is favourable, trading at similar levels to the benchmark globally and at a discount in Australia.

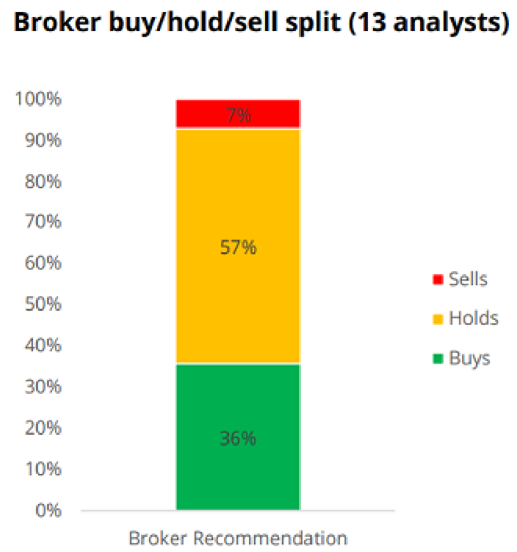
Scentre group (ASX:SCG)

Retail REIT Scentre Group finished middle of the pack over 12 months. February 2023 earnings results were operationally strong, reporting FFO of 20.06 cps (above guidance) and an occupancy rate of 98.9% (up from 20bps on the pcp). The group benefited from increased consumer visitations and visitation time. Looking ahead, high interest costs remain a headwind and are cautious given the likely slow-down in spending following the

RBA hiking cycle. However, Scentre Group is well equipped to manage an inflationary environment with specialty leases priced at CPI + 2%, providing scope for rental growth.



Source: Bloomberg, as at 28 February 2023



Source: Bloomberg, as at 28 February 2023

VanEck sees the emerging macro-economic environment, characterised by elevated inflation and low growth as the central scenario over the medium term. This environment is beneficial for real estate assets which offer inflation-linked revenue streams including exposure to subsectors that offer inelastic demand in an environment where the global economic activity is subdued.

Cameron McCormack is a Portfolio Manager at VanEck Investments Limited, a sponsor of Firstlinks. This is general information only and does not take into account any person's financial objectives, situation or needs. Any views expressed are opinions of the author at the time of writing and is not a recommendation to act.

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Market narratives are seductive and dangerous

James Gruber

In mid-1945, Tsutomu Yamaguchi was in Hiroshima in Japan for a three-month business trip. On the morning of August 6, he was preparing to leave the city with two colleagues for his hometown of Nagasaki when he realized he'd forgotten his identification papers, so he trekked back to his office to retrieve them. At 8.15am, the American bomber *Enola Gay* dropped an atomic bomb called 'Little Boy' near the centre of the city, about three kilometres from where Yamaguchi was walking.

Yamaguchi recalled that there was 'a great flash in the sky, and I was blown over'. The bomb blinded him temporarily, ruptured his eardrums, and resulted in radiation burns on the left-hand side of his body. He managed to gather himself and eventually find his colleagues, who also survived. They spent a night in an air-raid shelter before returning to Nagasaki the next day.

Yamaguchi received treatment for two days and went back to work at Mitsubishi Heavy Industries on August 9. At 11am on that day, he was describing the Hiroshima bombing to his supervisor when the American bomber *Bockscar* dropped an atomic bomb called 'Fat Man' over Nagasaki. Again, Yamaguchi was about three kilometres from where the bomb landed. This time, he didn't suffer any injuries, though he vomited and had a high fever for the next week.

Yamaguchi was only one of about 70 people who were affected by both bombs. Yet, he was the only person officially recognized by the Japanese government as having survived the two explosions.

Six days after the bombing of Nagasaki, Japan surrendered to the Allies, and World War Two was over by agreement on September 2.

The Hiroshima and Nagasaki bombs killed up to 226,000 people, mostly civilians. About half died on the days the bombs dropped, and many others died in the months after from radiation burns and illness.

Following the war, Yamaguchi worked as a translator for the occupation forces and later went back to Mitsubishi as an oil tank designer. By the 1980s, he became more strident in his opposition to atomic bombs. He called for the abolition of such bombs and for nuclear disarmament.

In 2009, when the Japanese government recognized him as a survivor of both bombs, Yamaguchi said:

"My double radiation exposure is now an official government record. It can tell the younger generation the horrifying history of the atomic bombings even after I die."

And Yamaguchi died aged 93 in 2010.

Tsutomu Yamaguchi

Source: Wikipedia

Why Yamaguchi's story is powerful

After surviving the bombs, Yamaguchi's life could have taken many paths. He could have wallowed in his wounds. He could have been bitter at America for their actions. He could have hated his own country for what happened.

Yet, amazingly, he worked for the Allies including the Americans, after the war. He also found a cause in fighting against atomic bombs and nuclear weapons. And he lobbied hard to be recognized by his country as a survivor of both bombs. Without this work, we may never have found out about his life.

Yamaguchi's survival story is an amazing one. Yet just as powerful is what he did after the explosions - he made the best out of a horrific situation.

We're story-telling animals

Tales like Yamaguchi's touch us because we're storytelling animals. We love to construct narratives around our own lives and the lives of others. These narratives are told after the event and can contain varying degrees of truth. And we particularly like stories like Yamaguchi's, where something bad happens, though it ends with a relatively happy ending (for him, at least).

Human beings have always told elaborate stories and tried to convince as many people as possible to believe in them. Bestselling author of *Sapiens*, Yuval Noah Harari, suggests storytelling is a large part of the reason why homo sapiens have come to dominate other species:

"Fiction has enabled us not merely to imagine things, but to do so collectively. We can weave common myths such as the biblical creation story, the Dreamtime myths of Aboriginal Australians, and the nationalist myths of modern states. Such myths give Sapiens the unprecedented ability to cooperate flexibly in large numbers. Ants and bees can also work together in huge numbers, but they do so in a very rigid manner and only with close relatives. Wolves and chimpanzees cooperate far more flexibly than ants, but they can do so only with small numbers of other individuals that they know intimately. Sapiens can cooperate in extremely flexible ways with countless numbers of strangers."

And Harari says stories are a way for us to give meaning to our own lives:

"Homo sapiens is a storytelling animal that thinks in stories rather than in numbers or graphs, and believes that the universe itself works like a story, replete with heroes and villains, conflicts and resolutions, climaxes and happy endings. When we look for the meaning of life, we want a story that will explain what reality is all about and what my particular role is in the cosmic drama. This role makes me a part of something bigger than myself, and gives meaning to all my experiences and choices."

Stories can have negative effects too. Harari argues that if you simply tell the truth, no one will listen. Consequently, you won't have any power because power comes from the stories you convince other people to believe. He says there will never be a society that values truth over power. And he gives examples of stories which can spread persecution, intolerance, and genocide. Nevertheless, Harari believes there are facts that are separate from fables and myths, and it's our job to find these facts.

Dan McAdams, a professor at Northwestern University in the US, has developed a psychological theory called 'narrative identity' to describe our ability to use storytelling to make sense of the world. The theory suggests that at an early age, people begin to become historians of themselves. They start to see their past as something they can make meaning out of and frame it in a way that helps them understand where they may be going in future.

From his research, McAdam has found life stories are associated with psychological wellbeing. For example, those who tell redemptive stories about their past – stories which transition from bad to good – tend to live more meaningful lives.

Separating market truth from fiction

Given humans drive markets, it's unsurprising that markets too are story-driven machines. Think about the narratives told at the start of 2022:

- Bitcoin and the rise of digital currency
- Sam Bankman-Fried, the billionaire face of this new economy
- Tech dominance
- The inexorable rise of venture capital and private equity
- The Fed will always save markets, aka the Fed Put
- 60/40 will always deliver
- Low interest rates are here to stay
- Inflation is transitory
- Russia will overrun Ukraine

These narratives turned out to be comically false by the end of last year. Yet they generated plenty of headlines during the preceding 12 months. Many of today's market 'truths' may also prove short-lived by the end of 2023.

We not only like to develop stories around markets but stocks too. There's the narrative around Australian companies that are taking on the world and winning. CSL is a good example of this (and valued at 36x forward P/E, it may need to take on other planets and win too). There are 'cool' stocks to own like Wesfarmers: after all, who doesn't love Bunnings? There are turnaround stories such as Myer and Whitehaven Coal. And there are stocks that investors kick when they're down – AMP and Zip, for instance.

With all the stories around markets and stocks, what is the average investors supposed to do? Well, it's the job of investors to do as Harari says, and that is separate truth from fiction. And to recognize what they can and can't control.

The truth lies in numbers. A company profit and loss statement is real; a balance sheet is real; and a cashflow statement is real.

In the long term, markets and companies are driven by earnings and the multiples attached to those earnings. If investors focus on these two things, they can ignore a lot of the white noise that surrounds them daily.

James Gruber is an Assistant Editor at Firstlinks and Morningstar. This article is general information and does not consider the circumstances of any investor.

Dealing with retirement anxiety

Richard Dinham

The last three years of a pandemic have taught us to expect the unexpected. It is also an apt lesson for anyone planning for retirement.

Fidelity International's latest retirement study - *New life, old life* - which surveyed over 1,200 Australians found that while the average age at which Australians would like to retire fully is 64.8 years, the average age we actually retire at is 63.4 years.

Furthermore, the average age at which Australian's plan to reduce their work commitments and transition into retirement is even younger, at 62.5 years, but the average age at which Australians start reducing their work commitments is 61.4 years.

So many of us are likely to transition into retirement somewhat earlier than expected and we will be fully retiring probably at least 12 months earlier than we had planned.

Some of the reasons for this earlier retirement are out of our control. The top three reasons cited for retiring earlier than planned were:

- personal health issues (one in four)
- redundancy (one in four) and
- needing to care for someone suffering from health issues (one in eight).

An unexpected early retirement can leave some people reeling in shock from which it may be difficult to recover. But if these people had planned ahead for the unexpected, if they had a Plan B already in place, that shock would likely be much less. They would be more resilient to the unexpected.

In fact, the Plan B is perhaps more important than the Plan A, given the potential impact it can have. So it's more important than ever to start thinking about retirement plans as early as possible.

Running out of money

Pre-retirees biggest fears is running out of money whilst in retirement and, closely related to this, the fear of not having enough income to live on.

How long your money will last in retirement essentially depends on three variables:

- how much you start with
- how much and when you draw income down from capital (spending)
- the characteristics of your investments.

When forced into early retirement, people don't have full control over their starting capital and it's probably less than they planned. But retirees do have control and agency over the other two variables.

Deferring or reducing expenditure could help sustain the savings pool for longer. This lever is often used by many retirees as they adapt to their lived experience of spending needs and wants, and their experience with investment outcomes. An important element of course is their lived experience of their investment portfolio. Retirees who have a plan in place and an investment framework for dealing with income needs, market volatility and maintaining suitable risk exposures, will likely feel more in control and more resilient to the inevitable gyrations of the investment markets.

Getting help with how to invest

For many people who are not familiar with financial markets, professional advice can be useful. The preferred source of professional advice on retirement, according to the Fidelity survey, is a professional financial adviser at 55%, followed by accountants at 23%.

But there are some barriers to accessing financial advice, with a large chunk of advisers leaving the industry during the last four years - up to 40% - and with each adviser seeing fewer clients now because of increased regulatory requirements, the cost of advice has also increased.

When it comes to reasons for not seeking financial advice, after a preference for doing it themselves or feeling confident they can manage their own financial affairs, not being able to afford financial advice is the reason most pre-retirees (28%) and retirees (30%) cite.

Other evidence suggests that existing clients of advisers may not be as price sensitive because they understand the good that financial advice does when it comes to addressing their retirement worries and concerns.

Addressing financial advice barriers

The Federal Treasury's Quality of Advice Review, released to the public in February 2023, has made some radical suggestions for improving access to financial advice. These recommendations are designed to reduce some of the administration and compliance burdens that currently rest with advisers and will hopefully reduce the barriers and the cost to getting advice.

The Government has not given any indication yet of what it will do with those recommendations. It is now consulting before bringing in any new regulation. There is widespread support for many of the recommendations although there is also some resistance from consumer groups who are concerned that consumer rights will not be protected appropriately.

According to research, the five most common questions pre-retirees have about retirement are:

- How much do I really need?
- Am I on track?
- What are my options?
- How much should I be saving today?
- What can I afford to spend in retirement?

Sitting down with an adviser and asking these questions could be beneficial to both the client and advisers looking to demonstrate the value of financial advice.

Changing goals

The good news is that once you have retired, anxiety levels usually drop as expectations change over time. How we judge a successful retirement changes as we age.

When asked what success in life means, only 37% of pre-retirees chose being financially successful as their key measure. And this drops to just 26% for early retirees. For those already in retirement, the best measures of having a successful and fulfilling retirement were *Being happy in yourself* at 84%, followed by *Doing what you love every day* at 64%. Early retirees were also more likely to see *Helping other people around you* as an indicator of success at 49%, compared to 44% of pre-retirees.

Also, many retirees are not big spenders. They often spend their time engaging in low-cost activities, including relaxing, time with family and friends, reading and engaging in hobbies and exercise.

Calming down

From the research study, it seems that once people enter retirement, settle into a new rhythm and come to a level of acceptance about their circumstances, their anxiety levels around their financial situation drops and they are better able to enjoy their retirement within their means.

Financial advice can play a very important role in improving life satisfaction in retirement, so let's hope that financial advice becomes more accessible for all.

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